BankDhofar بنك ظفار
Moving forward... with you معكم.. نتقدم

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بنك ظفار
BankDhofar

ANNUAL REPORT 2008

بنك ظفار
BankDhofar
Moving forward... with you

Contents

His Majesty Sultan Qaboos bin Said

Our Philosophy

Since the inception, BankDhofar with its philosophy of "Customer First" has developed a reputation for commitment, foresight and remarkable, yet solid, growth. BankDhofar believes in, and is committed to, maintaining relationships by offering personalised services to retail and corporate clients.

BankDhofar is committed to new ideas, innovation, revision and fine-tuning of its practices. The Bank continues to offer innovative products and services and implement creative strategies ahead of market trends to achieve sustained growth.

BankDhofar is well known for reliability as its foundation for service, based on advanced technology delivered by professional, competent and approachable staff. The Bank consistently demonstrates good faith and integrity in its dealings with all its stakeholders, providing acceptable returns to shareholders whilst maintaining a strong financial base.

BOARD OF DIRECTORS' REPORT

BANKDHOFAR S.A.O.G.
THE BOARD OF DIRECTORS' REPORT
For the year ended 31 December 2008

2008 Highlights

- *A new organisation structure for the Bank*
- *Launched our 5 year strategic plan (2008 - 2012)*
- *Selection of New Core Banking System*
- *Shareholders' Equity increased by RO 70.8 million through Rights Issue*

Dear Shareholders,

On behalf of the Board of Directors of BankDhofar S.A.O.G., I am pleased to present to you the Bank's Financial Statements and the Auditors' Report for the financial year ended 31 December 2008.

The Bank's Financial Performance in 2008

The Bank continued to achieve good results during the year 2008 despite the global financial crisis in the last quarter. The financial indicators reflected remarkable growth as the total assets increased from RO 955.13 million at the end of 2007 to RO 1,323.82 million in December 2008, a growth of 39%. The gross loans and advances improving by a healthy 42%, from RO 750.04 million at the end of 2007 to reach RO 1,068.77 million at the end of 2008. Also, the customer deposits raised by the Bank recorded an impressive growth of 44% and increased from RO 674.50 million at the end of 2007 to RO 971.60 million at the end of 2008.

Further, all the key profitability indicators achieved significant growth, as net interest income increased from RO 30.36 million during 2007 to reach RO 39.90 million during the year 2008 signifying a growth of 31%. Non-interest income such as fees and commissions, foreign exchange profit, investment income and other income grew by 19% and reached RO 16.27 million during 2008 compared to RO 13.68 million achieved in the previous year. We have reduced the cost to income ratio from 38.5% in 2007 to 37.6% in 2008, which indicates that our revenues grew at a better rate than our costs. The operating profit of the Bank as a result of the above factors grew by 29% from 27.08 million generated in 2007 to RO 35.06 million in 2008. The impairment due to prolonged and significant decline in market value of both local and global investments during the year ended December 2008 is RO 4.86 million and it has been charged off to profit and loss in accordance with the International Financial Reporting Standards.

The net profit for the year 2008 after the above charge and provisions for non-performing loans, grew by 4% to reach RO 23.69 million from RO 22.79 million achieved in 2007.The earnings per share (EPS) at the end of 2008 was RO 0.044 as compared to RO 0.043 in 2007.

Rights Issue

Our Bank successfully accomplished one of the largest rights issues in the local market to raise RO 70.77 million from the existing shareholders through issue of 176.9 million ordinary equity shares in December 2008. As per the Bank's business strategy the proceeds from this issue will be used to fund the planned current and future business growth. The shareholders' equity post-rights issue increased from RO 110.50 million at the end of 2007 to RO 188.43 million at 31 December 2008. In this regard we would also like to extend our sincere thanks to all our shareholders for the trust and confidence reposed in our Bank and for making this "Rights Issue" a grand success.

New Core Banking System

To enable the Bank's vision of transformation to reach the next level of business growth and customer service, the Bank has chosen Finacle Universal Banking Solution from Infosys. As part of this strategic initiative, the Bank would implement a New Core Banking system which will cover all banking activities, Customer Relationship Management, Treasury, Internet Banking and Mobile Banking Solutions for its operations and channels for the customers. The introduction of new age technology-based robust banking software would make the Bank more competitive and enable it to adopt world class banking practices to offer distinctive services to the customers.

Corporate Governance

The Bank has fully complied with all directives of the Code of Corporate Governance issued by the Capital Market Authority. Also during 2008 the Bank assessed and reviewed the internal control procedures of the Bank.

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 2008 as sitting fees was RO 71,800 and the proposed remuneration for the year is RO 128,200.

Proposed Dividends

The Board of Directors recommends 15.5% cash dividends amounting to RO 10.97 million, and a Bonus share issue of 4.5%, translating to 31,848,224 shares of RO 0.100 each, of the share capital of the Bank. We will also transfer an amount of RO 7.7 million to subordinated loan reserve as per the requirements of the Bank for International Settlement (BIS) for the purpose of Capital Adequacy Calculation.

The percentages of dividends distributed in the last five years is as follows:

Year	2003	2004	2005	2006	2007
Cash Dividends	15%	15%	10%	15%	25%
Bonus Shares	-	-	10%	15%	-

Acknowledgement

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 management of the Bank. I thank the shareholders for your continuous support and the Bank's staff and management for the good performance in 2008.

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 of the Bank, I would like to express our 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

BOARD OF DIRECTORS

Engineer Abdul Hafidh Salim Rajab Al Aujaili
Chairman

Sheikh Hamoud Bin Mustahail Ahmed Al Mashani
Vice Chairman

H.E. Ahmed Abdullah Sulaiman Moqaibel
Board Member

Mr. Saleh Nasser Juma Al Araimi
Board Member

Mr. Ahmed Bin Said Mohammed Al Mahrezi
Board Member

H.H. Sayed Taimoor Bin Asa'ad Al Said
Board Member

Mr. Ali Ahmed Al Mashani
Board Member

Mrs. Najah Musallim Sulaiman Al Kiyumi
Board Member

Mr. Mohammed Yousuf Alawi Al Ibrahim
Board Member

MANAGEMENT TEAM

Mr. Kris Babicci
Chief Executive Officer

Mr. Christopher De'Ath
General Manager Strategy & Planning

Mr. Mohammed Redha Ahmed Jawad
General Manager
Wholesale Banking

Mr. Abdul Hakeem Omar Al Ojaili
Deputy General Manager
Support Services

Mr. Ravi Khanna
Assistant General Manager
Information Technology

Mr. Faisal Hamed Sulaiman Al Wahaibi
Assistant General Manager
Consumer Banking

Mr. Bashir Said Al Subhi
Head of Treasury and International Banking

Mr. Emad Khalid Al Zubi
Assistant General Manager & Chief Financial Officer

Mr. Mohammed Yar Mohammed Al Balushi
Head of Human Resources

Mr. Ahmed Said Al Ibrahim
Assistant General Manager
Government Relations

Mr. Rajesh Kusumwal
Head of Internal Audit

Mrs. Huwayda Nasser Al Shahimi
Head of Corporate Communications & Marketing

Mr. Mohan Nair
Senior Manager Compliance

Mr. P.M. Ranganathan
Head of Risk Management

REPORT ON CORPORATE GOVERNANCE

Deloitte.

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TO THE SHAREHOLDERS OF
BANK DHOFAR SAOG

We have performed the procedures prescribed in Capital Market Authority (CMA) Circular No. 16/2003 dated 29 December 2003 with respect to the accompanying corporate governance report of **Bank Dhofar SAOG** and its application of corporate governance practices in accordance with CMA code of corporate governance issued under Circular No. 11/2002 dated 3 June 2002 and CMA Rules and Guidelines on disclosure, issued under CMA administrative decision 5, dated 27 June 2007. Our engagement was undertaken in accordance with the International Standards on Related Services to agreed-upon procedures engagements. The procedures were performed solely to assist you in evaluating the Bank's compliance with the code as issued by the CMA.

We report our findings as below:

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

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

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

Our report is solely for the purpose set forth in the first paragraph of this report and for your information and is not to be used for any other purpose, this report relates only to the accompanying corporate governance report of **Bank Dhofar SAOG** to be included in its annual report for the year ended 31 December 2008 and does not extend to any financial statements of **Bank Dhofar SAOG**, taken as a whole.

Deloitte & Touche

Deloitte & Touche (M.E.)
Muscat, Sultanate of Oman
28 January 2009

Corporate Governance Report

For the year ended 31 December 2008

Part One

1. Corporate Governance Philosophy

The Board of Directors of BankDhofar SAOG (the Bank) bears 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, bears the responsibility of strategic supervision of the Bank, apart from fulfilling statutory obligations. Some of the major responsibilities of the Board, namely audit, senior management succession, legal and regulatory compliance are discharged through four sub-committees, viz. the Executive Committee, the Audit Committee, the Risk Committee and the Human Resources Strategic 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 of the Bank. The Executive Management of the Bank comprises the Senior Managers headed by the Chief Executive Office.

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.

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. In the ultimate analysis, there can be no substitute for the enlightened self-regulation that is expected of every member of the Bank.

2. 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. Such authority shall not be limited or restricted except as provided by the law, the Articles of Association or resolutions of the General Meetings.

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.

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

Corporate Governance Report

For the year ended 31 December 2008

similar period. The term of the current Board expires in March 2010.

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 no 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, none of their immediate relatives having held a senior position in the Bank for the last two years, who shall have no relation with the Bank, its affiliated and sister companies that could result in financial transactions other than contracts and transactions entered through open tendering or done in the ordinary course of business.

The election process is through direct secret ballot whereby each shareholder shall have a number of votes 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 and are independent within the scope of the definitions laid down in the Code of Corporate Governance by the CMA.

Board Committees

The Board has the following four 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:

- Executive Committee
- Audit Committee
- Risk Committee
- Human Resources Strategic 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.

Part Two

1. Members of the Board of Directors

The Board of Directors of BankDhofar (SAOG) consists of the following:

Sr. No.	Name of Director	Basis of Membership			No. of Other Directorships Held
1	Eng. Abdul Hafidh Salim Rajab Al Aujaili	Chairman Non-Executive	Independent	Shareholder Director	1
2	Sheikh Hamoud Mustahail Ahmed Al Mashani	Vice-Chairman Non-Executive	Independent	Non-Shareholder Director	2
3	HH. Sayed Taimoor Bin Asa'ad Al Said	Member Non-Executive	Independent	Non-Shareholder Director	-
4	HE Ahmed Abdullah Sulaiman Moqaibel	Member Non-Executive	Independent	Non-Shareholder Director	3
5	Mr. Ali Ahmed Al Mashani	Member Non-Executive	Independent	Non-Shareholder Director	2
6	Mr. Mohammed Yousuf Alawi Al Ibrahim	Member Non-Executive	Independent	Non-Shareholder Director	2
7	Mr. Ahmed Said Mohammed Al Mahrezi	Member Non-Executive	Independent	Non-Shareholder Director	2
8	Mr. Saleh Nasser Juma Al Araimi	Member Non-Executive	Independent	Non-Shareholder Director	2
9	Mrs. Najah Musallim Al Kiyumi	Member Non-Executive	Independent	Non-Shareholder Director	-

The Board of Directors held 10 meetings during 2008 as follows:

- 16 January 2008
- 28 January 2008
- 23 March 2008
- 20 May 2008
- 25 June 2008
- 31 August 2008
- 17 September 2008
- 14 October 2008
- 8 November 2008
- 16 December 2008

Corporate Governance Report

For the year ended 31 December 2008

Sr. 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	10	10,000	17,990
2	Sheikh Hamoud Mustahail Ahmed Al Mashani	In Personal Capacity	9	8,400	11,990
3	HH. Sayed Taimoor Bin Asa'ad Al Said	In Personal Capacity	4	3,600	11,990
4	HE Ahmed Abdullah Sulaiman Moqaibel	Representative of Dhofar International Development & Investment Holding Company (SAOG)	9	7,800	14,989
5	Mr. Ali Ahmed Al Mashani	In Personal Capacity	9	6,400	11,990
6	Mr. Mohammed Yousuf Alawi Al Ibrahim	In Personal Capacity	8	8,200	13,489
7	Mr. Ahmed Said Mohammed Al Mahrezi	In Personal Capacity	10	8,900	14,989
8	Mr. Saleh Nasser Juma Al Araimi	Representative of Public Authority for Social Insurance	8	6,300	14,989
9	Mrs. Najah Musalim Al Kiyumi	Representative of Ministry of Defense Pension Fund	10	8,600	13,489
10	Sheikh Salem Mubarak Al Shanfari *	In Personal Capacity	2	1,200	765
11	Mr. Abdul Aziz Ali Al Shanfari *	In Personal Capacity	2	1,200	765
12	Eng. Saeed Salim Al Shanfari *	Representative of Dhofar Cattle Feed (SAOG)	2	1,200	765
			TOTAL	71,800	128,200

* Sheikh Salem Mubarak Al Shanfari, Mr. Abdul Aziz Ali Al Shanfari and Eng. Saeed Salim Al Shanfari were members of the Board of Directors up to end of January 2008.

2. Executive Committee

The Committee consists of four 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 Executive Committee are:

Name of Director	Designation	No. of Meetings Attended
Eng. Abdul Hafidh Salim Rajab Al-Aujaili	Chairman of the Committee	5
Mr. Ali Ahmed Al Mashani	Member	4
Mr. Ahmed Said Mohammed Al Mahrezi	Member	5
Mrs. Najah Musalim Al Kiyumi	Member	5

The Executive Committee held 5 meetings during 2008.

3. Audit Committee

The Audit Committee was formed in 2001 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).
- 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 foregoing 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 Audit Committee are:

Name of Director	Designation	No. of Meetings Attended
HE Ahmed Abdullah Sulaiman Moqaibel	Chairman of the Committee	6
HH. Sayed Taimoor Bin Asa'ad Al Said	Member	2
Sheikh Hamoud Mustahail Ahmed Al Mashani	Member	6
Mr. Mohammed Yousuf Al Ibrahim	Member	4

The Audit Committee held 6 meetings in 2008.

Corporate Governance Report

For the year ended 31 December 2008

4. Risk Committee of the Board of Directors

The Risk Committee of the Board was formed in October 2004 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 Risk Committee are:

Name of Director	Designation	No. of Meetings Attended
Mr. Saleh Nasser Juma Al Araimi	Chairman of the Committee	3
H.H. Sayed Taimoor Bin Asa'ad Al Said	Member	1
Mr. Mohammed Yousuf Alwai Al Ibrahim	Member	3
Sheikh Hamoud Mustahail Ahmed Al Mashani	Member	3

The Risk Committee held 3 meetings in 2008.

5. Human Resources Strategic Committee of the Board of Directors:

The Human Resources Strategic 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 Human Resources Committee are:

Name of Director	Designation	No. of Meetings Attended
Mr. Ahmed Said Mohammed Al Mahrezi	Chairman of the Committee	3
Mr. Mohammed Yousuf Alwai Al Ibrahim	Member	3
Mrs. Najah Musalim Al Kiyumi	Member	3

The Human Resources Strategic Committee held 3 meetings in 2008.

6. 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 2008 are as follows:

	Proposed Remuneration RO '000	Sitting Fees Paid RO '000	Total RO '000
Chairman of the Board	18.0	10.0	**28.0**
Board Members	110.2	61.8	**172.0**
Total	**128.2**	**71.8**	**200.0**

The Bank's top five executives, namely the Board of Directors Advisor, the Chief Executive Officer, General Manager – Strategy & Planning, General Manager – Wholesale Banking and Deputy General Manager- Support Services have received the following in 2008:

	Salaries RO '000	Performance Bonus & Others RO '000	Total RO '000
Top five Executives	**612.0**	**737.0**	**1,349.0**

7. 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 2007 when the Bank was penalised for RO 2,500 by one of its regulator. 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.

Corporate Governance Report

For the year ended 31 December 2008

8. Communication with Shareholders and Investors

The Bank publishes its quarterly interim financial statements and also hosts these and other relevant information at its website (www.bankdhofar.com). The quarterly results are published in two local newspapers in Arabic and English. These results can be obtained by shareholders either from the Bank or Muscat Securities Market (MSM).

The management provides regular updates to the market on the Bank's performance and new developments. The Management Discussion and Analysis Report forms part of this annual report.

9. Market Price Data

a. Share Price Movements

The high/low share price information of the Bank during the financial year ended 31 December 2008 compared with Muscat Securities Market Index is as follows:

2008	BankDhofar Share Price (RO)			MSM Index
Month	High	Low	Closing	Closing
January	0.705	0.620	0.665	9,172.11
February	0.795	0.670	0.777	10,362.81
March	0.830	0.765	0.806	10,102.57
April	1.000	0.835	0.806	11,210.97
May	0.950	0.850	0.917	11,554.69
June	1.100	0.880	0.894	11,323.04
July	0.910	0.710	0.756	10,737.10
August	0.800	0.635	0.660	9,493.75
September	0.700	0.545	0.564	8,493.56
October	0.564	0.370	0.393	6,209.96
November	0.450	0.342	0.438	6,263.86
December	0.421	0.329	0.370	5,441.12

b. Major Shareholders

The following are the major shareholders who own more than 5% of the outstanding shares as at 31 December 2008:

Shareholder	% of Ownership
Dhofar International Development and Investment Holding Company (SAOG)	30.90%
Civil Service Pension Fund	10.00%
Ministry of Defense Pension Fund	8.57%
Public Authority for Social Insurance	8.46%
Malatan Trading and Contracting LLC	7.45%
Qais Omani Establishment LLC	6.46%

10. Profile of the Statutory Auditors

Deloitte Touche Tohmatsu is an organisation of member firms around the world devoted to excellence in providing professional services and advice. Deloitte is focused on client service through a global strategy executed locally in over 140 countries. With access to the deep intellectual capital of approximately 165,000 people worldwide, Deloitte delivers services in four professional areas: audit, tax, consulting, and financial advisory services.

Deloitte & Touche in the Middle East is among the region's leading professional services firms, providing audit, tax, consulting, and financial advisory services through 25 offices in 14 countries with over 1700 partners, directors and staff. The Oman Practice currently has three partners and over 60 professionals.

11. Acknowledgement

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 internal rules and regulations.
- There are no material matters that affect the continuation of the Bank and its ability to continue its operations during the next financial year.

12. Other Matters

- During 2008 the Bank has fully complied with all directives of the Code of Corporate Governance issued by the CMA.
- The Statutory Auditors of the Bank are Deloitte Touche Tohmatsu. The Audit fees paid or payable to auditors for 2008 is RO 34,750.
- The last Annual General Meeting was held on 28 March 2008 and the last Extraordinary General Meeting was held on 14 October 2008.
- All board members attended the last Annual General Meeting.

THE MANAGEMENT DISCUSSION AND ANALYSIS REPORT

The Management Discussion and Analysis Report

For the year ended 31 December 2008

Oman's Economy and Outlook

The first three quarters of 2008 had been an extraordinary performance for Oman's economy where it experienced a nominal GDP growth in excess of 45% on average reaching a high of 52% in 3rd Quarter 2008 boosted by high average oil prices.

The average oil output in 2008 reached 756,000 barrels per day, an increase of 6.4% from 710,000 barrels per day in 2007 but short of the 790,000 bpd target set by the government in its 2008 budget. The budget surplus totaled RO 1.979 billion during January-November and this is expected to surpass the RO 2 billion mark by December, a record for the country's fiscal history. Higher oil output and prices pushed Oman's total revenue to an all time high of around RO 7.77 billion during the first 11 months of 2008, well above the total revenue of 2007, while oil export earnings account for more than 70% of total revenues at RO 5.439 billion.

The Muscat Securities Market (MSM), on the other hand, suffered a setback dropping 40% in 2008. The MSM gained 34% since the start of the year touching an all-time high of 12109.10 in June before dropping down to close at 5441.12 as a result of the financial and credit crisis worldwide leading to a free fall in commodities and equities. Oil prices tumbled more than 70% from the July peak of USD 145 per barrel which in turn affected the sentiment of the MSM index.

Going forward the Oman economy is expected to face a challenging year under the present economic condition worldwide as oil prices are expected to remain well below the 2008 average price of USD 95 per barrel. The government is taking a bold step to increase spending as compared with the budgeted total for 2008. The total expenditure for 2009 has been estimated at RO 6.4 billion as compared to RO 5.8 billion, an increase of RO 624 million or 11% from 2008. The 2009 budget projects a deficit of RO 810 million based on revenues of RO 5.6 billion and spending of RO 6.4 billion based on budgeted oil price of USD 45 per barrel while the government projects an economic growth of 1%. This is an important step as it signals a strong message to investors both within and outside that the government is committed to sustain the Oman economy against the backdrop and slump in oil prices and crippling global financial crisis.

Strategy & Planning

In 2008 BankDhofar established a new Strategy & Planning Department to guide the implementation of the Business Strategy (2008-2012) that had been developed in consultation with Booze Allen Hamilton in late 2007. The executive launched the strategy in a series of major 'town hall' meetings across Oman to communicate our new vision to be 'a leading Omani bank that everyone wants to work for, do business with and invest in.'

Throughout 2008, our management team and staff have demonstrated their commitment to our new strategic intent to transform into a high performance organisation and to outperform in growth and profitability. This commitment to a common goal was recognised in the Bank's financial results for 2008, despite the global financial crisis that has developed in the last quarter.

In 2008, our strategy called for a particular focus on the management of our human resources. Several important achievements are worth mentioning including the development of our Human Resources function through the recruitment of a number of talented professional staff, the establishment of a biannual performance review process, and the review of our remuneration strategy, including the establishment of a new profit participation scheme. This focus on our people will continue in 2009 with significant investment in our training programs to ensure that staff have the skills required to develop professionally and deliver further strong results for the Bank.

Looking forward, our strategic focus will be on the development of our technology and business processes, while continuing to focus on the recruitment and development of our people.

Corporate Communications & Marketing

As a result of our new strategy, 2008 also saw the establishment of a new Corporate Communications and Marketing function within the Bank aimed at improving the Bank's profile in the marketplace. We have enhanced our corporate branding and visibility; our branches now are more customer friendly and have adopted a new look. The department also has worked on enhancing our communication within the Bank and externally with our customers.

Wholesale Banking Group

In line with the recommendations made by Booze Allen Hamilton, an organisational restructuring was carried out in 2007 and 2008 as a result of which the Wholesale Banking Group was created consisting of the Corporate Banking Department, Project Finance & Syndications Department, Small & Medium Enterprises (SME) Department, Remedial, Trade Finance Sales and Corporate Advisory & Structured Finance Departments.

The rationale behind this change was to focus on segmentation of the Corporate market and provide the full range of Corporate services under a single umbrella. During the year staffing of key positions was taken through induction of highly qualified and trained professionals.

In the backdrop of a rapidly changing economic profile of the country, increased competition in the sector and the evolving banking regulatory regime, we believe that the Wholesale Banking Group will spearhead the future growth for the Bank. It is our objective to be the 'Bank of choice' for corporate customers in Oman and cater to all their banking requirements and services. To achieve this the Bank is continually streamlining internal procedures, removing bottle-necks and hiring experienced professionals committed to deliver corporate banking services of the highest standard. The Bank is also currently upgrading its technological platform for providing efficient delivery channels to its Corporate customers which include the provision of internet-based banking facilities.

In 2008, despite the visible downtrend in some of the economic sectors all the lending arms of the Wholesale Banking Group have performed exceedingly well. This was possible due to leveraging of the existing relationships to increase our exposure to the extent possible, growth in new Corporate and SME lending, growth in the Project Finance/Syndicated Loan portfolio and growth in overseas lending. Also we have been able to lend to companies with larger fund requirements in consortium with regional banks.

Corporate Banking Department

The Corporate Banking Department provides Corporate Banking products – both funded and non-funded and has been instrumental in developing the Bank into a 'Relationship Bank'. Typical products extended by the department include term loans of various maturities both for capital expenditure and working capital requirement, Letters of Credit, Loans against Trust Receipts and Guarantees. The customer base of the Corporate Banking Department, spans over a wide range of industries including Trading, Manufacturing, Services and Contracting. Depending on the industry sector, the banking products are suitably devised to effectively cater to the particular requirement of the sector.

Every customer or a group of customers is assigned a specialist relationship executive, who is in constant touch with the customers to understand their requirements and offer suitable services and products on most competitive terms. The emphasis is on the development of individual financial solutions that are suited to the particular needs of the customers. The executive also liaises with other departments of the Bank to facilitate prompt delivery of the required services and products to the satisfaction of the customer. The Bank considers these relationship executives as vital links with its customers. The department has also embarked upon supporting the Relationship Team with a team of dedicated Credit Analysts, which will drastically improve the turnaround time to the customers and will also improve the control mechanism substantially.

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As a part of the Bank's increased emphasis on Trade Finance, a special cell has been created to attend to specialised requirements of the customers in this area. The objective is to have a continuous interaction with the customers in order to provide effective solutions in the area of Trade Finance. The department has already witnessed a jump in the business volumes and revenue in 2008 and the trend is expected to continue in 2009 as well.

Project Finance & Syndications Department

In line with the Government of Oman's continuing initiative a number of projects of national importance, requiring considerable investment are being implemented at a rapid pace. BankDhofar has taken a conscious decision to actively participate in financing of these projects within its exposure norms. Accordingly, a separate department had been carved out to focus on these opportunities which requires specialised skills and close interaction with other local and international banks.

Over the years the Bank has participated in several important local projects including the projects of Oman India Fertiliser Company LLC, Sohar Aluminum, Oman LNG, Oman Gas, Salalah Port, Oman Refinery (expansion), Octal Petrochemicals and the six power and water projects. The Bank has in place the technical capability to independently lead-arrange funds for mid-cap projects and has a strategic tie-up with regional and international banks for the purpose of ensuring full participation. A start in this direction has been made with lead-arranging the funds for various projects taken up by reputed companies. Realising the lending potential across the border the Bank has increased its participation in respect of cross-border deals within the permitted regulatory ceiling. The Bank is also making a foray into the provision of Advisory Services for Projects and Corporates and is in the process of building a suitable team.

Going forward over the long term we envisage a host of lending opportunities in the Infrastructure, Oil & Gas, Construction and Tourism sectors taking into account the large Government sponsored projects as well as those privately sponsored. However, against the backdrop of the current global economic and financial crisis we expect a slowdown in the launching of new projects especially in the first half of the year.

Mid Sector Corporate Division & Business Banking Unit

The Mid Sector Corporate Division & Business Banking Unit has recently been set up as the SME division in the Bank. The growth in the economy of the country has witnessed rapid growth of the Small & Mid Corporate sector in particular. With the Bank laying more emphasis on these growing sectors in the economy, the division has been formed with a focus to cater specially to growing Mid Corporate sector, while the business banking unit shall cater to the requirements of smaller business units.

Professional account relationship managers are appointed to assess the needs of the customers and provide solutions tailor-made to their requirements. The Bank has been able to provide the finance needs to this sector with our products ranging from Funded to Non-Funded, from Short-Term to Long-Term and from Credit to Trade Services, ensuring that the customers get finance the way it is best suited for their businesses. The account relationship managers also facilitate the customer's access to the Bank's other products and services.

The division endeavours to provide best services to the customers with faster turnaround time, while maintaining the quality of the assets of the Bank. Special attention is provided to the evaluation of the credit proposals and the risk assessment for each borrower.

Over a longer term this particular segment shall witness growth commensurate with the growth of the country's economy. The focused approach for this particular segment shall enable the Bank to reap the benefits arising out of the growth in the segment.

Consumer Banking Group

Distribution Network

It was an outstanding year for the Consumer Banking Division (CBD) of BankDhofar, as it continued its focus on providing value-added products and services to the

customers. The Bank continued its growth and expansion strategy in 2008, strengthening its distribution channels with the addition of more branches, ATMs and Deposit & Bill Payment Machines (DBPMs).

The year 2008 saw the addition of 2 new branches at Mabellah and Salalah Gharbiya, relocated 2 branches – Al Khuwair and Azaiba, renovated the Muttrah Souq Branch, installed 6 ATMs (4 offsite ATMs) and 13 Deposit & Bill Payment Machines (3 of which were installed at Omantel and OmanMobile outlets in Bhaja, Awqadain Salalah & Ibri). The year ended with 51 branches, 91 ATMs and 21 Deposit & Bill Payment Machines.

Products

Al Heson

The year also saw the growth of BankDhofar's flagship scheme Al Heson savings scheme offering bigger and better prizes to its customers. The Al Heson savings scheme is one of the most popular savings schemes in the market with its unique proposition which gives customers the opportunity to open an account and get the chance to win every fortnight.

The Al Heson scheme continued its promise of offering more prizes every fortnight, and draws for bi-monthly, quarterly. All this along with other special prizes and draws for various segments and age groups in the form of gold for ladies and a Mazen & Mazoon draw for children.

Card Centre

2008 saw a tremendous growth in the credit cards business – both in terms of new customers as well as outstandings. A successful campaign coupled with an exciting contest was conducted for branches and direct sales staff, which helped in this growth.

The new Chip Credit Card introduced in 2007 was well received by customers. This chip card has both the magnetic strip as well as chip functionality. The chip functionality offers BankDhofar's Chip Credit Card users complete security and greatly enhances the procedure of fraud detection at terminals that are chip-enabled. The Chip Credit Card is offered on both Visa and MasterCard platforms. Along with security the Bank's credit cards come with various benefits and advantages like privileged access to Oman Air Airport lounge at Muscat and Salalah, free travel insurance including accident, baggage and flight delay for card holder and family, interest-free repayment period of up to 52 days, emergency card replacement, etc.

Special value additions for customers were introduced in 2008. This included a tie-up with the Royal Orchid Lounge at the Bangkok International Airport, and a tie-up with Al Shatti Cinema offering free movie tickets to BankDhofar credit card holders on Fridays. These benefits were publicised and well received by the customers.

Housing Loans

Our housing loan product was further enhanced with more flexibility, hence qualification is not limited to monthly salary but other additional income is also taken into consideration. Another category of housing loan product for businessmen and the self-employed has been introduced. The customer can also mortgage more than one property to qualify for a housing loan. The product is very competitive in the market as it offers a low monthly installment, and low insurance. It also comes along with a free credit card. Housing loans are available to customers to buy, build or renovate their homes. Loans are also made available for buying a plot of land or investing in residential projects. In the year 2008 housing loans were availed by more customers than the previous years.

Outbound Sales

The Outbound Sales Department consists of Direct Sales Agents and the Call Centre.

The Outbound Sales Department focused on an expansion of the team across the country. New direct sales teams providing home banking service (opening of accounts and loans in the convenience of customers' homes and offices) were launched in Salalah, Sohar and Sharqiah regions. The team strength was increased in the capital region to take advantage of the growing market. Frequent training programmes on products and sales were conducted. As a

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result, new customers were brought into the bank, and the Direct Sales Team of BankDhofar is a reckoning name in the market today.

Call Centre services were also improved through enhanced training and introduction of service monitoring tools, such as mystery shopping and call quality scoring. The Call Centre strength was increased to 14 call agents under a supervisor and a manager. Call Centre also generated an increased amount of business through inbound and outbound customer calling. For the benefit of our customers the Call Centre now operates 24 hours a day and 7 days a week. In the period of last 12 months, the Call Centre has witnessed a significant increase in the number of calls being handled by staff - from about 60,000 calls to about 90,000. These call volumes are apart from the volumes of credit card calls and the volumes handled by the IVR.

Treasury & International Banking Division

Customer focus has been one of the key areas of the Treasury department's business strategy. The Bank provides a high level of service to its Treasury customers through up-to-date information about products and markets. The Treasury Division offers a wide range of treasury-related services to all of our valued corporate, retail and high net worth individual customers. The other major functions of the Treasury are to control the interest rate risk for reserve holding, exchange rate risk, and liquidity management on a daily basis, with a view to enhance yield.

We are one of the leading market contributors in USD/OMR spot and swaps prices. We offer attractive interest rates on deposits in all major currencies to corporate, retail and high net worth individual clients. We also offer highly competitive exchange rates against all major currencies for spot and forward requirements of our clients.

The Treasury and International Division performed well in 2008. Foreign Exchange income grew by 42% as compared to the 2007 figures. During 2008, investment in international and regional T-Bills, currency swaps, and corporate relationships with increased business from trade-related activities played a major role in the robust growth.

The division is planning to set up a dedicated structured product desk that will cater to the sophisticated business community requirements. The desk will provide various hedging tools, structured in combination of products such as Interest Rate Swap (IRS), Floating Rate Agreements (FRAs) and Options.

International Banking Division continued to focus its efforts to develop mutual beneficial relationships with financial institutions worldwide. Through a large network of correspondents, BankDhofar facilitates international business of its retail, corporate and institutional clients at competitive rates with a greater emphasis on quality services. The division also supports and assists in the areas of trade finance, foreign exchange and building relationships with financial institutions globally. Despite the economic turmoil in the financial markets worldwide the division was responsible for arranging a bilateral loan of USD 20 Million for 3 years from ING Bank, Netherlands during the last quarter of the year at a competitive pricing.

The Bank's credit ratings from the three international credit rating agencies are as follows for the year 2008.

Moody's Investor Service affirmed A3/P-2 local currency rating, A3/P-2 foreign currency deposit rating, and a D+ Bank Financial Strength Rating (BFSR) to our Bank. The outlooks on all ratings are stable. Fitch Ratings affirmed our Bank's rating at long-term issuer debt (IDR) "BBB+" with a stable outlook and short-term IDR "F2", individual "C", support "2" and support rating floor "BBB+". Cyprus-based "Capital Intelligence (CI) affirmed our Bank's foreign currency long-term and financial strength ratings at "BBB" and the foreign currency short-term rating at "A3". The support rating is unchanged at 3 and the outlook for all the ratings remains "Stable".

Government Relations and Investment Management

The Government Relations Department provides valuable support for the resource mobilization and marketing initiatives of the Bank. The Investment Management Department offers Brokerage and Asset Management Services. It serves a diversified client base, including pension funds, corporations, high net worth individuals and retail clients. The team comprises investment professionals with several years of experience, who are flexible and responsive to our clients needs. Our Asset Management Division currently manages discretionary and non-discretionary investment portfolios. Despite the stock market turmoil which negatively impacted investor confidence during the last quarter of 2008, the department through its disciplined approach to investing during bull or bear phases, managed to perform better than the benchmark Muscat Securities Market (MSM) Index.

Backed by strong research and asset management capabilities, the team plans to build up the size of assets under management during the coming year. The Brokerage Division managed to garner additional institutional business. It currently offers brokerage services on the Muscat Securities Market and plans to expand this service to other GCC markets by entering into strategic tie-ups with brokerage houses in other GCC markets. The Brokerage and Asset Management Divisions are supported by the Research Division which provides research covering the Oman market, as well as a Back Office which serves the clients reporting requirements. The Back Office was also involved in the IPOs and rights issues during 2008, for which our Bank was the collecting banker.

Support Services

Central Operations Division

2008 was a challenging year with the commencement of the implementation of the Business Process Re-engineering project by the Strategy & Planning Department and Central Operations Department. The department continues to be associated in implementing several key projects such as Cheque Imaging System (CIS), E-banking and Core Banking besides the Business Process Re-engineering (BPR). Along with these projects, Central Operations Department has been continuously working on streamlining many work-flows aimed at reducing the operational burden at the branches and eliminating operational errors.

The volume of transactions processed at COD continued to grow steadily. The key reason for this was the continuous focus by the team to effectively utilise technological solutions to automate routine processes thereby increasing the productivity of the team. This also resulted in the ability of the team to handle the increasing volume of transactions, efficiently.

Prior to commencement of Business Process Re-engineering project (BPR), the Senior Manager, Central Operations Department along with the Quality Assurance Manager, visited several banks in GCC countries and India to have a first hand understanding of the BPR project, undertaken by these banks and the benefits on its implementation.

Key Achievements

The following are some of the areas in which we have streamlined the workflow at the Bank, through automation and centralisation:

- Automation of Inward Real Time Gross Settlement remittances.
- Automation of charges on issue of cheque books.
- Automation of follow-up on minors' accounts when they attain the age of maturity.
- Automation of follow-up of 'Stop-Payment' instructions.
- Introduction of operations manual on standing instructions.

Trade Finance Department

Trade Finance Department provides fund based credit facilities such as Export Bills discounting and import financing to our customers as well as non fund based credit facilities like Letters of Credit for Imports and Issuance of Guarantees. During the Year 2008, the Bank registered more than 100% growth in off-balance sheet business viz, Letters of Credits and Guarantees. In an increasingly competitive market, the only sustainable path for this achievement is through customer satisfaction. Our Bank could achieve this target by providing quality customer service and commendable turnaround time. To meet the challenges in a turbulent international market, our Trade Finance team guided our customers with their valuable advice and placed necessary

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checks and balances to avoid fraudulent claims by overseas traders. This year, International Chamber of Commerce (ICC) introduced new rules in the Trade Finance field viz., Uniform Customs & Practices (UCP600), International Standard Banking Practices (ISBP) and Uniform Rules for Reimbursements. Our Trade Finance team, comprising mainly of Omani staff, successfully assimilated these developments and provided quality customer service

Key Achievements in 2008

- Above 100% growth in off-balance sheet business thereby contributing to the growth of Bank's fee based income without strain on Capital requirement.
- Substantial reduction in turnaround time in Issuance of Guarantees and Letters of Credit by introducing standard templates and training of operational staff.
- Elimination of fraudulent claims by international traders by taking timely precautionary measures.

Future Plans

- Implementation of Trade Finance Module in Finacle Core Banking Solution and Internet Banking.
- Increasing the skills and expertise of local staff by providing cross-functional training to staff as well in new ICC Rules.

Credit Control

In compliance with the directives of Central Bank of Oman on best risk management practices, the Bank has established Credit Control Department (CCD) in 2007 under Support Services Group. This department was formed with the objective of strengthening of credit risk management processes through independent review of loan portfolio so as to bring about the qualitative improvement in loan administration and control on an ongoing basis.

The Department is entrusted with the responsibility of implementation of Loan Review Mechanism (LRM), approved by the Bank's Board. LRM is a comprehensive and independent credit review process, distinct from Risk Management and Internal Audit functions. The scope of LRM covers evaluation of credit risk assessment and approval processes, adherence to loan policies/procedures, sufficiency of loan documentation, overall quality of post-disbursement follow up/loan administration, identification of early warning signals, independent review of risk grading and provisioning in respect of large, unsecured and critical borrower accounts handled by Corporate Banking, Project Finance & Syndication and Small & Medium Sector under Wholesale Banking Division.

Reviews are conducted within three months of the grant of credit facilities. Findings of such reviews are presented to the Management Credit Committee at its weekly meetings on an ongoing basis by independent evaluation of various credit processes. Such reviews facilitate the concerned departments to undertake timely corrective measures. All major findings and important observations are reported to the Board. In terms of regulatory guidelines, at least 30% of the Corporate loan portfolio is to be subjected to LRM in a year. However in 2008, CCD had conducted reviews of around 70% of credit facilities sanctioned by various authorities for large and critical accounts in Wholesale Banking Division.

CCD also conducts portfolio reviews to ensure compliance with various norms on advances as prescribed in the Bank's Credit Risk Policy approved by the Board. Since inception, CCD has taken up review exercises to clean up the loan database in the system, to improve the quality of MIS reports by modification of IT programmes. In line with the objectives, CCD would continue to play an important role in reviewing and strengthening various credit risk management processes and in supporting implementation of the new Core Banking Solution.

Information Technology

In line with the strategic plan the Bank has chosen latest technology based state-of-the-art computer system for Core Banking, Treasury, Customer Relationship Management (CRM), Internet Banking and Mobile Banking for its operations and additional channels for the customers. The new computer system would help the Bank to offer new and innovative products to the customers and would make the Bank more competitive. This solution would transform our branches to customer centric outlets and enable the Bank to adopt world-class banking practices to offer differentiated services to the customers. It will help the Bank to further increase operational efficiencies through business events automation and process orchestration eliminating manual tasks resulting in faster turnaround and processing time.

CRM module of the solution will offer a 360 degree view of the customer, comprehensive and rich customer support service facilities for Opportunity Management, Campaign Management and Incident Management. The full functionality treasury module of the solution would enable the Bank to enhance its Treasury operations. The Bank will offer Internet Banking services to Corporate and Retail customers.

Information Technology division has upgraded the Bank's pioneer SMS Banking channel to offer Arabic Pull, Arabic Bulk Messages, Online Bill Payments and Pre-paid Mobile Top-ups. The Bank introduced additional 10 cash Deposit and Bill Payment machines by offering new functionalities such as Mobile Top-ups and Enquiry for bills. The division consolidated databases for various applications reducing database management effort and improving the availability of systems.

Leveraging the power of Business Intelligence Tool 'Business Objects', the division has developed a large number of analytical reports on historical data-enabling business divisions to extensively use these analytical reports for taking strategic and business decisions.

As part of the strategic plan, the Bank has selected the new generation ATM Switch solution to support the various business requirements such as Europay MasterCard VISA (EMV) CHIP Acquiring, EMV CHIP issuing for debit cards, Internet enabling of our debit cards, enabling of balance enquiry on International VISA ATMs. This will help deliver better customer service to our debit card holders. The new solution will improve services offered from ATM channel and provide better MIS and reporting. It will also help the Bank to comply with the major International Payment Network mandates on EMV, 3DES Security, improved Fraud Monitoring Controls and Payment Card Industry Data Security Standards (PCI-DSS) Compliance.

The Bank signed the agreement for moving its Wide Area Network to Multi Protocol Label Switching (MPLS) technology to enhance security and improve network bandwidth for its branches and ATMs.

The division completed the implementation of the revised Information Security Policies and Procedures across all Head Office Departments. The Bank has completed the development and implementation of Information Security Management System (ISMS) framework in the IT Division based on ISO/IEC 27001 standards. An ISMS is a part of the overall management system, based on a business risk approach, to establish, implement, operate, monitor, review, maintain and improve information security. The ISMS includes organisation structure, policies, planning activities, responsibilities, practices, procedures, processes and resources.

Human Resources

Human Resource Management (HRM) is an approach to the management of an organisation's most valued assets - the people who individually and collectively contribute to the achievement of the objectives of the business. To achieve this, BankDhofar's HR Department has hired additional management staff (Manager – Recruitment & Career Development, Manager – Performance Management and Compensation, Manager – Training and Manager – Payroll and Administration).

Human Resources at BankDhofar have been integral to our sustainability and undoubtedly, our success has been a testament to the excellence we have within the Bank. We are always identifying, recruiting and developing promising young Omanis and providing them great career opportunities in banking. We pride ourselves for being able to maintain the Omanisation ratio above the stipulated limit at 91% in the year 2008. This demonstrates our commitment towards grooming the local talent.

The total staff strength of the Bank increased from 720 in 2007 to 840 by the end of 2008 to support the Bank's expansion. Several HR initiatives were implemented largely to ensure that the collective effort of the organisation is further strengthened.

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New Graduate Development Program

A Graduate Development Program was launched in October to train and develop young Omani graduates to pursue banking careers with emphasis on their strength and acquired knowledge from their respective field of studies. A career development path has been mapped and will be put into action in 2009. To further build up on this endeavour, career plans are already on the final planning stage. The training department has been active in providing simultaneous training sessions within all sectors of the organisation while classes have been conducted at the College of Banking & Financial Studies to accommodate the classroom requirement of the New Graduate Program.

On-Line Assessment

Aimed to eliminate and reduce human error, HR is now in its final phase in the introduction of the On-Line Assessment as part of the recruitment process. This will ensure that applicants throughout the country will be afforded the same type of approach in their pre-employment testing through the On-Line Assessment tool.

Welcome Kit

We've all heard the expression; "First impressions aren't easy to erase." This statement holds true in talent acquisition where, according to recent study, 86% agree that new hires make their decision about whether or not to stay at the company within the first six months on the job. The pressure for organisations to retain talent they worked hard to recruit and hire has never been greater, and is driving the vast majority of all organisations surveyed to pursue through on-boarding process. BankDhofar HR Department is focused to make "On Boarding" part of any strategy that is focused on workforce retention and productivity, as well as brand management. It is envisioned that we should begin the on boarding process before the actual employment start date and what better way to initiate it than by presenting a well designed Welcome Kit. We see the "Welcome Kit" as an excellent initiative to present the Bank to the new employee.

HR Department will endeavour at its best to ensure that BankDhofar fulfill its destiny to become the "Employer of Choice".

Risk Management

a. 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. Board has set risk policies, limits and procedures by assessing the risk bearing capacity of the Bank.

The overall risk management has been assigned to an independent Risk Committee of the Board of Directors (RC) of the Bank, which monitors and controls the overall risk profile of the Bank. The RC reports to the full Board, on matters of significance and keeps the Board updated with the Risk Management process in the Bank. In this task RC relies on an independent Risk Management Division.

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 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 of the Bank and in ensuring that policies and procedures are tailored to the defined tolerance levels.

b. Risk Management Strategy

The risk management strategy of the Bank pivots on the following:

- To understand, measure and manage risk and aim at ensuring sustained growth of a healthy asset portfolio.
- Well-defined and disciplined risk measurement processes and procedures through well documented authority levels and limits.
- Continuous monitoring and control of these limits at business unit level and at portfolio level.
- Updating various authorities on risk profile of the Bank and suggest ways for risk mitigation.

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

1. 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 dealing with customers of good credit standing, a thorough and professional credit assessment, obtaining collaterals and continuous monitoring of the conduct of the account. Bank has also in place a Credit Risk Policy which encompasses organisational responsibilities, prudential limits, credit risk rating standards, risk pricing standards, loan review mechanism, delinquent account management and portfolio management.

The Bank employs experienced and competent staff in the areas of corporate banking, 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.

2. Liquidity Risk

Liquidity Risk is the potential inability of the Bank to meet it's maturing obligations to a counter party. Liquidity planning and management are necessary to ensure that the Bank has the ability to fund it's liquidity requirement effectively and to meet current and future potential obligations such as loan commitments, contingent liquidity commitments and unexpected deposit outflows.

While the Bank's Asset-Liability Committee (ALCO) is responsible for setting the broad framework for managing the liquidity risk effectively, the responsibility of managing the liquidity risk of the Bank, within this framework, lies with the Treasury Division which discharges this function with the assistance of other business divisions of the Bank.

The Bank has Board approved policy 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. A mid-office cell in the RMD ensures that the Bank operates within these guidelines. Mid-office cell has also implemented ALM software which monitors the liquidity position of the Bank and helps in managing the liquidity gaps, well in time.

3. 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 and interest rate risk.

The major foreign currency in which the Bank deals on a regular basis is the US Dollar. The established parity between US Dollar and Rial Omani substantially reduces this risk. However, in order to control currency exposure risk, limits for intra day and overnight positions have been set up in addition to currency wise stop loss limits. The Central Bank of Oman (CBO) has also set prudential norms for the net open position to restrict the banks from taking undue currency exposures.

The Bank manages the interest rate risk by matching the re-pricing of assets and liabilities and operating within the set gap limits. Foreign currency loans are linked to LIBOR (London Inter-bank Offered Rate) and re-priced regularly to reduce the attendant interest rate risk.

4. Operational Risk

Operational risk is the risk of loss resulting from inadequate or failed internal systems, processes, 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. Trained and

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competent staff oversee the various operational functions of the Bank. Tested and up-to-date disaster recovery plans exist to provide normal banking services in the event of any unforeseen disruption to business. The Bank has also issued detailed guidelines to the operating units and branches on identifying potential operational risks and to put in place appropriate key controls to mitigate such risks.

Risk Management Division (RMD) also conducts regular training programmes for staff at various levels to inculcate 'risk awareness' and to spread the general 'risk management culture' in the Bank.

c. Initiatives: For further enhancement in the risk management process:

- The Bank has the Moody's Risk Advisor (MRA) credit rating model, a globally reputed credit analysis tool that aids in assessing the credit risk in lending proposals. The Bank developed a new credit risk rating framework to assess the credit risk of the borrower objectively. The revised system of grading, shall be further strengthened to take into account the collaterals available, which can be used in pricing the loan assets. In addition to risk grading, the corporate credit proposals are reviewed by the RMD whose observations form an important input in the credit risk management process.
- The Bank has implemented a front-end software package for effective Asset and Liability Management. The system shall provide error-free data for effective liquidity gap management and interest rate risk.
- A system to conduct stress test with assumed stress/worst case scenarios of credit risk, interest rate risk, foreign exchange risk and equity price risk on a quarterly basis is in place to assess the impact on the Bank's capital adequacy and profitability under these stress scenarios. Besides regular stress tests, the Bank conducts various tests to understand the impact of current economic scenarios on its portfolio.

d. Basel II

CBO directed that banks operating in the Sultanate of Oman are required to do computation of their capital adequacy under Basel II with effect from 1 January 2007. As per the CBO directives, the Bank has adopted the Standardised Approach for Credit Risk and the Basic Indicator Approach for Operational Risk. The Bank is confident that with the Risk Management Processes established within the Bank and their continued upgradation, the Bank will assume more advanced approaches of Basel II to adopt best risk management practices and improve the quality of the assets on its books.

Financial Performance

Despite the global financial unrest during the last quarter of the year the Bank continued to achieve good results throughout 2008. The total assets of the Bank crossed the "One Billion" mark to reach RO 1,323.8 million as compared to RO 955.12 million at the end of 2007 signifying a sustained growth of 38.6%. The gross loans and advances to customers stood at RO 1,068.7 million as compared to RO 750 million at the end of 2007 reflecting a double digit growth of 42.49%.

An analysis of our loans and advances portfolio as at 31 December 2008 along with the comparative figures for the prior period is as follows:

Particulars	RO Million	
	2008	2007
Overdrafts	102.5	73.1
Loans	873.8	621.8
Loans against trust receipts	67.8	38.2
Bills discounted	3.5	3.2
Advance against credit cards	7.9	4.7
Others	13.2	9.0
Gross loans and advances to customers	**1,068.7**	**750.0**
Less: Allowance for impairment	50.3	45.4
Net Loans and Advances	**1,018.4**	**704.6**

The ratio of total non-performing advances (NPA) to gross loans reduced to 3.55% at the end of 2008 from 4.85% at the end of 2007 due to concerted efforts from all the departments concerned. Bad debts coverage ratio was healthy at 132.5% at end December 2008.

There was creditable growth of 44.04% in customer deposits from RO 674.5 million at the end of 2007 to RO 971.6 million at the end of 2008. This reiterated the trust and confidence reposed by the customers in our Bank.

The composition of customer deposits at the end of 2008 along with the corresponding figures for the prior period is as follows:

Particulars	RO Million	
	2008	2007
Current accounts	197.5	178.1
Saving accounts	163.9	142.9
Time deposits	606.5	351.4
Margin accounts	3.7	2.1
Total customer accounts	**971.6**	**674.5**

Shareholders' Equity

Our Bank accomplished one of the largest rights issues in the local market raising a capital of RO 70.77 million through issue of 176.9 million ordinary equity shares to its existing shareholders. As a result, the shareholders' equity at the end of 2008 increased to RO 188.4 million from RO 110.4 million at the end of 2007. At the end of 2008 an amount of RO 2.37 million was transferred to legal reserve being 10% of net profit. The subordinated bonds reserve balance of RO 7.36 million was added back to retained earnings as the bonds matured during the current year. Further, an amount of RO 7.7 million was transferred to subordinated loan reserve.

The analysis of shareholders' funds at the end of 2008 along with the corresponding figures for the prior period is as follows:

Particulars	RO Million	
	2008	2007
Share capital	70.77	53.08
Share premium	58.51	5.43
Legal reserve	14.61	12.15
Subordinated bonds reserve	-	7.36
Subordinated loan reserve	10.27	2.57
Proposed distribution-cash	10.97	13.27
Proposed distribution-bonus shares	3.18	-
Investment reserve revaluation	0.24	3.58
Retained earnings	19.88	13.06
Total Shareholders' Equity	**188.43**	**110.50**

As a result of the increase in shareholders' equity the net assets per share reached RO 0.266 at the end of 2008 compared with RO 0.208 at the end of 2007.

Income Statement

Particulars	(RO '000)	
	2008	2007
Net Interest Income	39,899	30,356
Fees and Commissions	4,245	2,774
Other Income	12,020	10,910
Operating Income	**56,164**	**44,040**
Total Operating Costs	**(21,105)**	**(16,964)**
Operating Profit	35,058	27,076
Net Profit	**23,686**	**22,790**

The Bank achieved good results in all key areas. The net interest income earned until December 2008 improved significantly by 31.44% to reach RO 39.9 million for the year ended 2008 from RO 30.36 million for the year ended 2007. Non-Interest income increased by 18.9% and reached RO 16.27 million at the end of 2008, net fees/commissions and profit from foreign exchange recorded growths of 53% and 34.04% respectively. As the stock markets across the world started tumbling from the last quarter of 2008, the

The Management Discussion and Analysis Report

For the year ended 31 December 2008

investments were marked to market and the impairment was charged off to the income statement. The total impact in the income statement due to impairment was RO 4.86 million.

Although the total operating expenses increased by 24.41% from RO 16.96 million in 2007 to RO 21.105 million in 2008, the cost to income ratio improved to 37.6% as compared to 38.5% last year, indicating better increase in revenue over costs.

The amount of additional provisions for impaired loans made in 2008 was RO 5.4 million and the recovery from provisions was RO 2.35 million.

The net profit in 2008 grew by 4% reaching RO 23.69 million compared with RO 22.79 million in 2007. The earning per share (EPS) increased from RO 0.043 in 2007 to RO 0.044 in 2008.

The Board of Directors proposed to pay 15.5% cash dividend amounting to RO 10.97 million and 4.5% bonus shares amounting to 31,848,224 shares of RO 0.100 par value each amounting to RO 3.2 million. Also the Bank will carve RO 7.70 million to be transferred to subordinated loan reserve.

The proposed profit appropriation for 2008 is provided in the following table:

Particulars	(RO '000)	
	2008	2007
Proposed dividends-cash	10,970	13,271
Proposed dividends-bonus shares	3,185	-
To legal reserve	2,369	2,279
To subordinated bonds reserve	-	1,474
To subordinated loan reserve	7,700	2,567
From/To retained earning	(538)	3,199
Net Profit for the year	**23,686**	**22,790**

Future Prospects

The Bank has in place strategic measures on a proactive basis to address the global financial crisis. The Bank's strong financial performance since its inception gives us the confidence of further business stability in 2009.

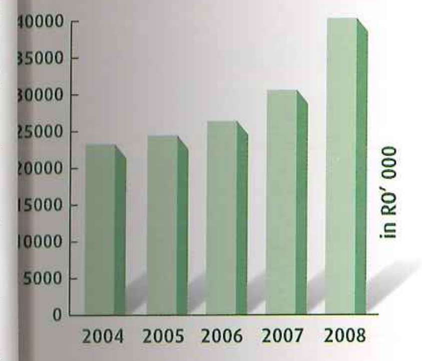
Financial Highlights of Last Five Years

(In RO '000) For the year	2008	2007	2006	2005	2004
Net Interest Income	**39,899**	30,356	26,245	24,396	23,264
Non-Interest Income	**16,265**	13,684	8,675	5,584	5,187
Operating Costs	**21,105**	16,964	13,614	13,170	12,497
Operating Profit (before impairment losses)	**35,059**	27,076	21,306	16,810	15,954
Profit From Operations	**27,077**	25,355	21,976	16,131	12,600
Net Profit for the year	**23,686**	22,790	20,130	14,199	11,078
At year-end					
Total Assets	**1,323,820**	955,127	694,799	618,225	551,293
Net Loan Portfolio	**1,018,441**	704,643	548,819	470,937	406,503
Customer Deposits	**971,596**	674,502	497,142	452,132	421,093
Shareholder's Equity	**188,433**	110,498	93,281	79,405	67,771
Share Capital	**70,774**	53,082	46,158	41,962	41,962
Full Service Branches	**51**	49	47	47	47
ATMs	**91**	85	79	79	66
Staff	**840**	720	636	598	579

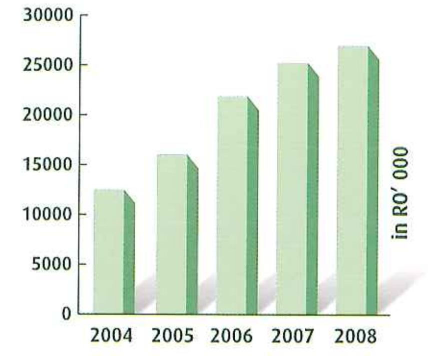
Financial Ratios of Last Five Years

	As at 31 December 2008	As at 31 December 2007	As at 31 December 2006	As at 31 December 2005	As at 31 December 2004
I- PROFITABILITY					
Return on Weighted Average Equity	**21.15%**	22.37%	23.31%	19.30%	16.90%
Return on Weighted Average Capital	**44.34%**	45.93%	45.68%	33.80%	26.40%
Return on Average Assets	**2.08%**	2.76%	3.07%	2.40%	2.20%
Non-Interest Income to Operating Income	**28.96%**	31.07%	24.84%	18.60%	18.20%
Operating Expenses to Operating Income	**37.58%**	38.52%	38.99%	43.90%	43.90%
II - LIQUIDITY					
Net Loans to Total Deposits	**95.97%**	91.75%	96.61%	91.90%	89.20%
Total Customer Deposits to Total Deposits	**91.55%**	87.83%	87.52%	88.30%	92.40%
III - ASSET QUALITY RATIOS					
Loan Loss Provisions to Total Loans	**4.71%**	6.05%	7.71%	8.60%	9.50%
Non-Performing Loans to Total Loans	**3.58%**	4.88%	7.00%	7.70%	8.30%
Loan Loss Provisions to Total Non-Performing Loans	**131.57%**	123.96%	110%	112%	114%
IV - CAPITAL ADEQUACY					
BIS Risk Asset Ratio	**16.63%**	14.87%	13.10%	15.30%	15.30%
BIS Risk Asset Ratio on Tier One Capital	**13.59%**	10.08%	11.66%	13.10%	13.00%
Shareholder's Equity/ Total Assets	**14.23%**	11.57%	13.40%	17.80%	12.30%

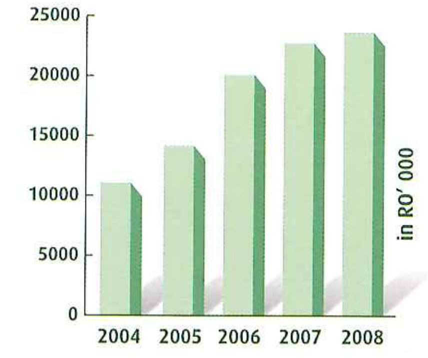
Financial Highlights of Last Five Years



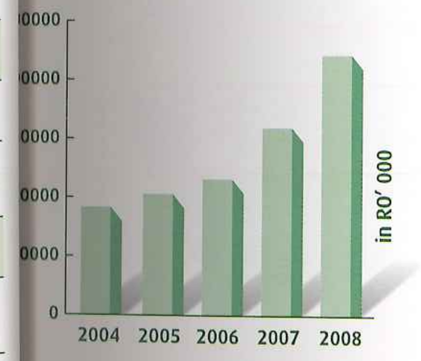
NET INTEREST INCOME



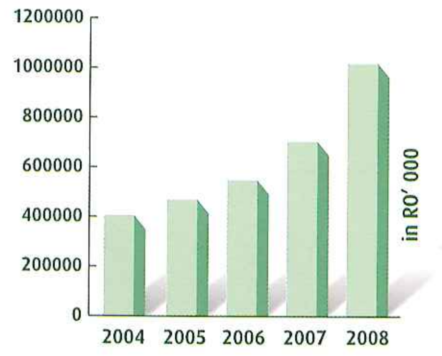
PROFIT FROM OPERATIONS



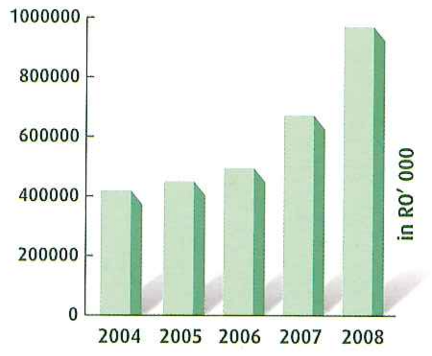
NET PROFIT FOR THE YEAR



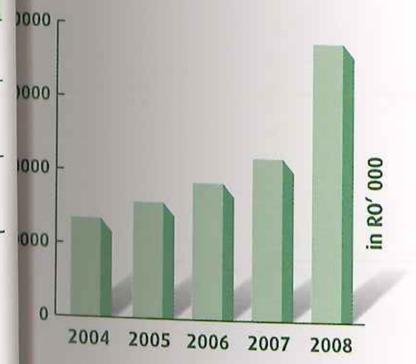
TOTAL ASSETS



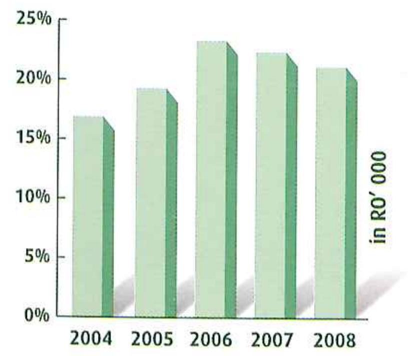
NET LOAN PORTFOLIO



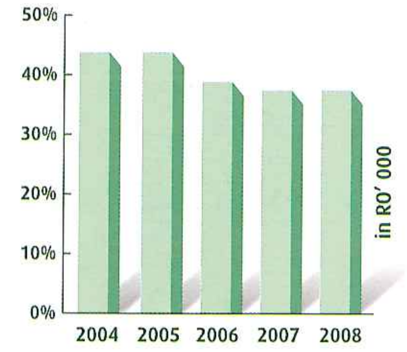
CUSTOMER DEPOSITS



SHAREHOLDER'S EQUITY



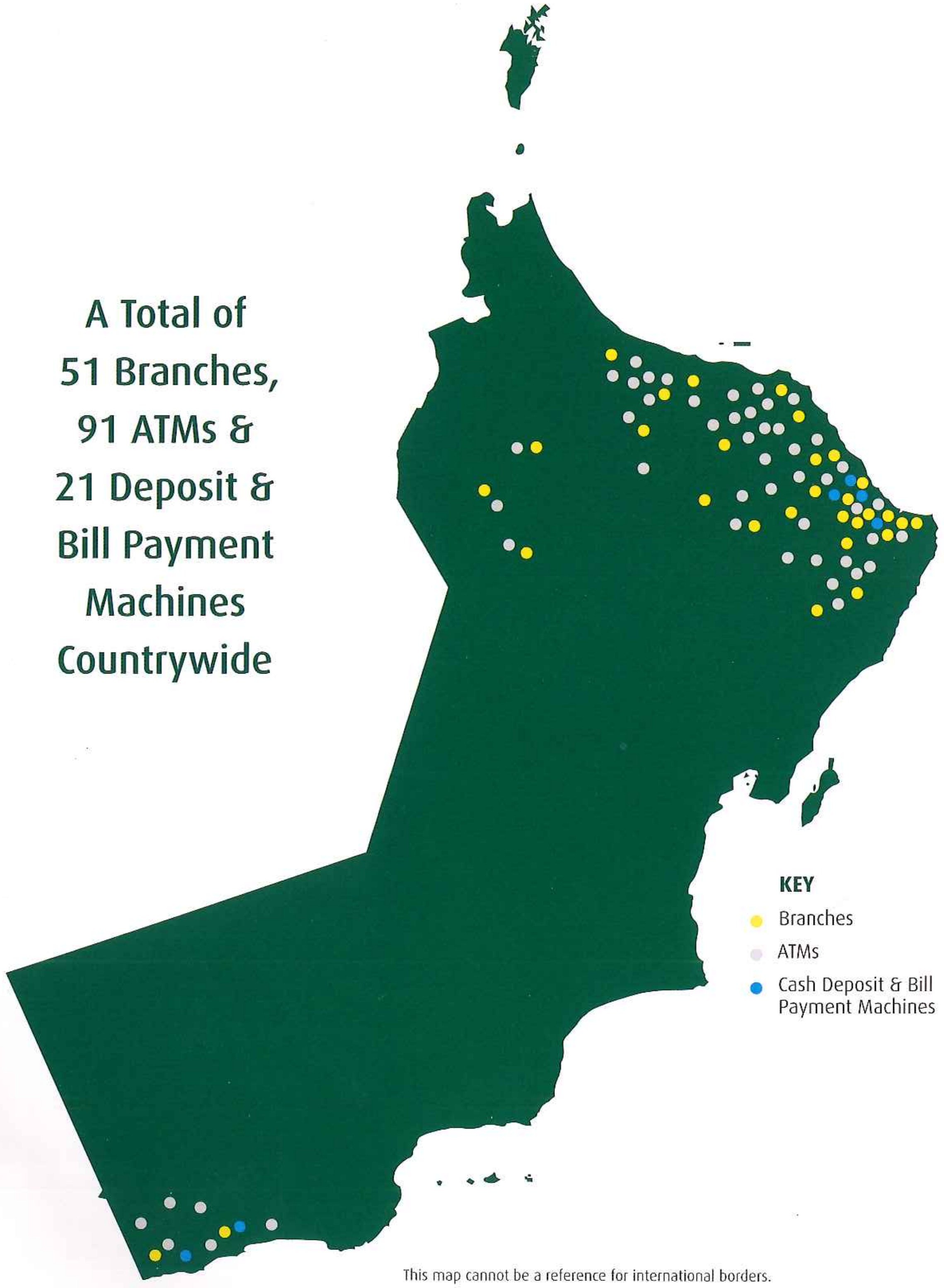
RETURN ON AVERAGE EQUITY



OPERATING EXPENSES TO OPERATING INCOME

Branches, ATMs & Cash Deposit & Bill Payment Machines

A Total of 51 Branches, 91 ATMs & 21 Deposit & Bill Payment Machines Countrywide



This map cannot be a reference for international borders.

BankDhofar Branch Network Contact Details

NO.	BRANCH	TEL. NO.	FAX NO.	P.O. BOX
MUSCAT		24701080 - 24790466 Ext: 406 / 421	24701090	1831, PC 112 Ruwi
1	Azaiba	24527295 - 24527291 - 24527292 - 24527293	24527296	378, PC 133 Al Khuwair
2	Al Khuwair 2	24484880 - 24480008 - 24485554	24483366	2717, PC 112 Ruwi
3	Al Khuwair	24475090 - 24475701 - 24475702	24488574	1507, PC 112 Ruwi
4	Al Khuwair Ministry	24694710 - 24694725 - 24694715	24694730	1591, PC 130 Aziba
5	Bausher	24502606 - 24596994	24595323	148 PC 130 Azaiba
6	Khoudh	24536132 - 24545026 - 24542826	24545268	1507, PC 112 Ruwi
7	Mabellah	24451539 - 24451540 - 24451520	24451542	1507, PC 112 Ruwi
8	Seeb Airport	24510101 - 24510537 - 24510102	24510468	56, PC Seeb PC 111
9	Seeb Town	24425851 - 24425852 - 24424434 - 24423373	24425627	347, PC 121 Al Seeb
10	Amarat	24876580 - 24876120	24875829	346 PC 119 Amerat
11	Greater Muttrah	24793297 - 24707959 - 24706636	24706103	1831, PC 112 Ruwi
12	Muscat	24737865 - 24736614 - 24736606 - 24737066	24739166	1613, PC 114 Muttrah
13	Muttrah	24712970 - 24714452 - 24714279	24713556	1441, PC 112 Ruwi
14	MBD	24750516 - 24790466	24798621	1507, PC 112 Ruwi
15	Qurum	24568351 - 24567671 - 24567673	24567679	108, PC 114 Muttrah
16	Quriyat	24845195 - 24845193 - 24845192	24845173	145, PC 120 Quriyat
17	Ruwi	24835854 - 24831090	24831892	1442, PC 112 Ruwi
18	Wadi Kabir	24814127 - 24814126	24814128	1507, PC 112 Ruwi
19	Wattayah	24565137 - 24566731 - 24565208	24566732	1507, PC 112 Ruwi
BATINAH & BURAIMI		26845562 - 26840228	26845512	21, PC 311 Sohar
1	Buraimi	25655647 - 25651696 - 25651989	25651115	278, PC 512 Buraimi
2	Barka	26884423 - 26884428	26884451	751, PC 320 Barka
3	Falaj Al Qabail	26750156 - 26750928 - 26751378	26750891	209, PC 322 Falaj Al Qabail
4	Hafeet	26817646 - 26817991 - 26817992	26817993	596 PC 319 Saham
5	Khadhra	26714164 - 26714162	26714163	505, PC 315 Al Suwaiq
6	Khaboura	26801686 - 26801028	26805130	423, PC 326 Khaboura
7	Suwaiq	26862001 - 26862010	26862102	585, PC 315 Suwaiq
8	Saham	26854400 - 26856699	26855277	92, PC 319 Saham
9	Sohar	26841712 - 26840794 - 26840228	26841229	21, PC 311 Sohar
10	Shinas	26748302 - 26748306 - 26748308	26748304	434, PC 324 Shinas
11	Al Ghashab (Rustaq)	26878737 - 26875759	26878797	216, PC 329 Burg Alradah
12	Muladdah	26868544 - 26868553	26868549	106 PC 341 Muladdah
13	Rustaq	26876039 - 26875117	26875591	25, PC 318 Rustaq
DHAKHLIYA & DHAHIRA		25410234 - 25411370	25411234	83, PC 611 Nizwa
1	Araqi	25695071 - 25694126	25695047	90, PC 515 Iraqi
2	Barkat Al Mauz	25443466 - 25443460	25443462	97, PC 616 Barkat Al Mauz
3	Bahla	25420021 - 25420292	25420387	661, PC 612 Bahla
4	Bid Bid	25369254 - 25369044 - 25369033	25369055	307, PC 613 Bid Bid
5	Izki	25340393 - 25340089 - 25341016	25340204	412, PC 614 Izki
6	Ibri	25692283 - 25689341 - 25689685	25690341	28, PC 511 Ibri
7	Nizwa	25410234 - 25411370	25411234	83, PC 611 Nizwa
8	Sumail	25351283 - 25351188	25350094	199, PC 620 Samail
SHARQIYA		25571756 - 25571658	25570253	514, PC 413 Ibra
1	Al Ees Sur	25545867 - 25544350 - 25541912	25543710	323, PC 411 Sur
2	Ibra	25571632 - 25571631	25570646	514, PC 413 Ibra
3	J. B. B. Ali	25553440 - 25553414	25553446	10, PC 416 Jalan
4	Kamil Al Wafi	25557134 - 25557501	25557962	294, PC 412 Al Kamil
5	Mintrib	25583853 - 25584049	25583510	154, PC 421 Bediya
6	Sinaw	25524663 - 25524367	25524823	296, PC 418 Sinaw
7	Sur	25546677 - 25541255 - 25540256	25540615	75, PC 411 Sur
8	Samad A'Shan	25526736 - 25526529	25526574	123, PC 423 Samad
DHOFAR		23292299 - 23294863 - 23291631	23293505	2334, PC 211 Salalah
1	Al Wadi	23211130 - 23212185 - 23212180	23210085	2334, PC 211 Salalah
2	Saada	23225463 - 23225409	23225179	2334, PC 211 Salalah
3	Salalah	23290644 - 23292299 - 23294863 - 23291631	23295291	2334, PC 211 Salalah
4	Salalah-Al Gharbiah	23297526 - 23297536 - 23298046	23295084	2334, PC 211 Salalah

Locations - ATMs, Cash Deposit & Bill Payment Machines

Location
MUSCAT
Muscat Branch ★
Muttrah Branch ★ ■
MBD Branch ★ ■
Greater Muttrah ★
Wadi Kabir Branch ★ ■
Ruwi Branch ★ ■
Amerat Branch ★
Wattaya Branch ★
Qurum Branch ★ ■
Al Khuwair Branch ★ ■
Mabellah Branch ★
Al Khuwair Centre Branch ★
Al Khuwair Ministry Branch ★
Sarooj ●
Al Maha Filling Station-Al Khuwair ●
Al Khuwair - Pick & Save ●
Bausher Branch ★
Azaiba Branch ★ ■
Seeb Airport Branch ★ ■
Seeb International Exhibition ●
Markaz Al Bahja ● ◎
Al Khoudh Branch ★ ■
Al Khoudh - Omanoil Filling Station ●
Al Mawaleh South-Shell Filling Station ●
Seeb Town Branch ★ ■
Azaiba, Shell Filling Station ●
City Center Lobby Mawaleh ●
Mercure Al Falaj Hotel, Ruwi ●
Al Maha Souk - Ruwi (Hamriya R/A) ●
Al Maha Souk - Amerat ●
Al Maha Souk - Ansab ●
Al Maha Souk - Wattaya ●
Al Maha Souk - Ghubra ●
Al Maha Souk - MSQ ●
Al Maha Fuel Station - Wadi Al Lawami Seeb ●
Muscat International Airport ●
Al Maha Fuel Statoin - Mawleh (Near Wave Project) ●
City Center Lobby Qurum ●
BATINAH
Barka Branch ★ ■
Rustaq Branch ★
Al Ghashab Branch ★
Muladah Branch ★
Suwaiq Branch ★
Al Khadhra Branch ★
Khaboura Branch ★ ■
Hafeet Branch ★
Saham Branch ★
Sohar Branch ★ ■
Shinas Branch ★
Falaj Al Qabail Branch ★
Falaj Al Qabail Drive thru ●
Sohar University, Sohar ●
Al Maqasa Souk, Hafeet ●
Al Maha Souk, Musannah ●
Al Tarif Souk, Sohar ●
Al Maha Souk - Al Hazem, Rustaq ●
Al Maha Souk - Al Waqaiba, Sohar ●
DHAHIRAH
Ibri Branch ★
Al Iraqi Branch ★
Buraimi Branch ★
Buraimi Drive Through ●
OmanTel Ibri ◎
DAKHILIYA
Bid Bid Branch ★
Samail Branch ★
Izki Branch ★
Barkat Al Mauz Branch ★
Al Shafaa - MOD ●
Nizwa Branch ★
Bahla branch ★
Al Maha Souk - Falaj Dariz, Nizwa ●
SHARQIYA
Sinaw Branch ★
Samad A'Shan ★
Ibra Branch ★ ■
Mintrib Branch ★
Al Kamil Al Wafi ★
J.B.B.Ali Branch ★ ■
Al Ees Branch ★
Sur Branch ★
Mudhaibi ●
DHOFAR
Salalah Branch ★ ■
Salalah Shell Filling Station ●
New Salalah - Al Najaf Street ●
Al Qoaf - Salaam Store ●
Haffa - Sultan Qaboos Street ●
Saada Branch ★
Dahareez ●
Al Wadi Branch ★ ■
Shell Filling Station, Al Salam Street ●
Al Awqadain ●
Al Isteqrar Hypermarket ●
Al Maha Fule Station, Al Saadah ●
Salalah Al Gharbiah Branch ★ ■
Omantel Awqadeen, Salalah ◎

LEGENDS

★ BRANCH
● OFF-SITE ATM
■ CASH DEPOSIT MACHINE
◎ BILL PAYMENT MACHINE

REPORT ON BASEL II-PILLAR III DISCLOSURE REQUIREMENTS

Deloitte.

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Muscat International Centre
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P.O. Box 258, Ruwi
Postal Code 112
Sultanate of Oman

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Tel: +968 24815896
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www.deloitte.com

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

We have performed the procedures agreed with you and as prescribed in the Central Bank of Oman ("CBO") Circular No BM 1027 dated December 4, 2007 with respect to the Basel II - Pillar III disclosures (the disclosures) of the **Bank Dhofar SAOG** (the Bank) set out on pages 47 to 57 as at and for the year ended December 31, 2008. The disclosures were prepared by the management in accordance with the CBO's Circular No. BM 1009 dated September 13, 2006 and Circular No. BM 1027 dated December 4, 2007. Our engagement was undertaken in accordance with the International Standard on Related Services applicable to agreed-upon procedures engagements. The procedures, as set out in Circular No. BM 1027 dated December 4, 2007, were performed solely to assist you in evaluating the Bank's compliance with the disclosure requirements set out in CBO's Circular number BM 1009 dated September 13, 2006.

We report our findings as follows:

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

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

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

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

Deloitte & Touche

Deloitte & Touche (M.E.)
Muscat, Sultanate of Oman
28 January 2009

BASEL II - PILLAR III DISCLOSURE

For the year ended 31 December 2008

DISCLOSURE REQUIREMENTS UNDER PILLAR – III OF BASEL II.

1. Disclosure Policy

The following detailed qualitative and quantitative public disclosures are provided in accordance with Central Bank of Oman (CBO) rules and regulations on capital adequacy standard Basel II issued through circular BM 1009 on September 13, 2006. 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 Bank has an approved disclosure policy to observe the disclosure requirements set out by the Central Bank of Oman and any other regulatory authority, and, International Financial Reporting Standards (IFRS) and International Accounting Standards (IAS).

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

a. To maintain capital adequacy ratio (CAR) at a minimum of 10%;

b. To adopt the standardised approach for credit risk for implementing Basel II, using national discretion for:
   - Adopting the credit rating agencies as external credit assessment institutions (ECAI) for claims on sovereigns and banks;
   - Adopting simple/comprehensive approach for Credit Risk Mitigants (CRM)
   - Treating all corporate exposures as unrated and assign 100% risk weight.

c. To adopt standardised 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.

2. Scope of Application

Bank has no subsidiaries or significant investments and Basel II is applied at the Bank level only.

3. Range of Disclosures

3.1. Capital Structure

BankDhofar's capital structure consists of Tier I capital and Tier II capital.

The capital base for complying with capital standards are quite distinct from accounting capital. The regulatory capital is broadly classified into three categories – Tier I, Tier II and Tier III.

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). Bank has increased its Tier I capital in the month of December 2008 through right issue by RO 70.86 million.

Tier II (supplementary capital) consists of undisclosed reserves, revaluation reserves/cumulative fair gains or losses 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 comprises of 45% of investment revaluation reserve and a general provision 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.

BASEL II - PILLAR III DISCLOSURE

For the year ended 31 December 2008

The details of capital structure is provided as under:

TIER I CAPITAL :	RO'000 Amount
Paid-up capital	70,774
Legal reserve	14,612
Share premium	58,506
Subordinated loan reserve	10,267
Retained earnings	19,880
Proposed bonus shares	3,185
Less goodwill	(3,971)
Cumulative unrealized losses recognized directly in equity	(753)
TOTAL TIER I CAPITAL	**172,500**
TIER II CAPITAL	
Investment revaluation reserve (45% only)	442
General Provision (Max of 1.25% of total risk weighted assets)	14,990
Subordinated Loan	23,100
TOTAL TIER II CAPITAL	**38,532**
TOTAL ELIGIBLE CAPITAL	**211,032**

3.2 Capital Adequacy

Bank has adopted Standardised Approach (SA) for computation of capital charge for credit risk and market risk, and Basic Indicator Approach (BIA) for operational risk. Under Standardised Approach for credit risk, Bank has adopted simple approach for recognising collaterals in the Banking Book and for risk weighting the claims on sovereign and banks, credit ratings of Moody's, S&P or Fitch is used. Assessment of capital adequacy is carried out in conjunction with the capital adequacy reporting to the CBO.

Bank has capital adequacy ratio of 16.63% as against the CBO requirement of 10%. The Bank's policy is to manage and maintain its capital with the objective of maintaining strong capital ratio and high rating. 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 capitalised at all times.

The Bank has in place a capital adequacy framework by which the Bank's annual budget projections and the capital required to achieve the business objectives are linked in a cohesive way. Capital requirements are assessed for credit, market and operational risks. The Bank's capital adequacy ratios are periodically assessed and reported to the Risk Committee (RC) of the Board of Directors. Bank also conducts various stress tests and observes its impact on capital, to ensure capital adequacy. The composition of capital in terms of Tier I, II and III are also analysed to ensure capital stability and to reduce volatility in the capital structure.

i) Position of various Risk Weighted Assets are presented as under:

Sr. No.	Details	Gross Balances (Book Value) RO'000	Net Balances (Book Value)* RO'000	Risk Weighted Assets RO'000
1	On balance sheet items	1,401,395	1,329,593	1,043,047
2	Off balance sheet items	141,360	123,082	123,013
3	Derivatives	3,782	3,782	1,256
4	Total Credit Risk	**1,546,537**	**1,456,457**	**1,167,316**
5	Market Risk			**16,064**
6	Operational Risk			**85,899**
7	Total Risk Weighted Assets	**1,546,537**	**1,456,457**	**1,269,279**

* Net of provisions, reserve interest and eligible collaterals

ii) Detail of Capital Adequacy:

Sr. No	Details	RO'000
1	Tier 1 Capital	172,500
2	Tier 2 Capital	38,532
3	Tier 3 Capital	-
4	**Total Regulatory Capital**	**211,032**
5	Capital Requirement for Credit Risk	116,732
6	Capital Requirement for Market Risk	1,606
7	Capital Requirement for Operational Risk	8,590
8	**Total Required Capital**	**126,928**
9	Tier 1 Capital Ratio	13.59%
10	Total Capital Ratio	16.63%

3.3 Risk Exposure and Assessment

The risks to which banks are exposed and the techniques that banks use to identify, measure, monitor and control those risks are important factors 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) 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 minimise the probable losses and maintaining credit risk exposure within acceptable parameters.

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 benchmarks, limits for management of credit risks. Continuous review of the credit policy is done to keep it in line with the business environment and regulatory requirements at all times.

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. 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 Risk Management Division through a system of independent risk assessment of credit proposals beyond a threshold limit of RO 100,000 before they are considered by the appropriate approving authorities. This facilitates the approving authorities in making informed credit decision. In addition RMD approves/reviews grading of obligors, and conducts regular analysis of the credit portfolio.

Bank also has 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.

Bank has in place a risk grading system for analysing the risk associated with credit. The parameters, while risk grading the customers, include financial condition and performance, quality of disclosures and management, facility structure, collateral and country risk assessment where necessary. 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 approval of CBO is obtained.

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For the year ended 31 December 2008

Retail lending is strictly in accordance with the CBO guidelines. In addition to these, there are also country limits approved by the Board to ensure portfolio diversification in terms of sovereign risk ratings and geographical exposure. Specific country risk limits have been set up based on the external ratings of the countries. Bank counterparty exposures are restricted to 25% of the country risk limits. All lending decisions are made after giving due consideration to credit policy requirements.

However, in the absence of acceptable external credit rating agency in the Sultanate of Oman, the Bank has obtained the 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. Every corporate account is reviewed annually and in case of special mentioned category accounts, reviews are conducted at higher frequency.

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 categorised 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.

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

Sr. No.	Type of Credit Exposure	Average Gross Exposure		Total Gross Exposures	
		RO'000	RO'000	RO'000	RO'000
		As at 31 December 2008	As at 31 December 2007	As at 31 December 2008	As at 31 December 2007
1	Overdrafts	**88,351**	68,968	**102,577**	73,052
2	Loans	**763,481**	549,138	**873,808**	621,846
3	Loans against trust receipts	**57,226**	36,583	**67,791**	38,203
4	Other	**11,688**	10,029	**13,180**	8,998
5	Bills purchased/discounted	**3,453**	2,068	**3,466**	3,224
6	Advance against credit cards	**6,244**	4,268	**7,945**	4,717
7	**TOTAL**	**930,443**	**671,054**	**1,068,767**	**750,040**

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

Sr. No.	Type of Credit Exposure	Oman	Other GCC Countries	*OECD-Countries	India	Pakistan	Other	Total
		RO'000	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
		1	2	3	4	5	6	7
1	Overdrafts	102,577	-	-	-	-	-	102,577
2	Personal loans	398,349	-	-	-	-	-	398,349
3	Loans against trust receipts	67,255	536	-	-	-	-	67,791
4	Other loans	456,371	17,383	1,705	-	-	-	475,459
5	Bills purchased /negotiated	3,466	-	-	-	-	-	3,466
6	Any other	21,125	-	-	-	-	-	21,125
7	**Total**	**1,049,143**	**17,919**	**1,705**	**-**	**-**	**-**	**1,068,767**

Overdraft and others included personal overdraft and others
*excluding countries included in column 2

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

Sr. No.	Economic Sector	Overdraft	Loans	Bills purchased	Others	Total	Off balance sheet exposures
		RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
1	Import Trade	10,454	40,643	116	30,418	81,631	40,214
2	Export Trade	69	124	-	-	193	188
3	Wholesale & Retail trade	6,108	10,504	-	3,597	20,209	2,949
4	Mining & Quarrying	930	34,195	-	329	35,454	664
5	Construction	11,219	29,800	-	19,790	60,809	89,058
6	Manufacturing	11,769	33,070	3,350	22,644	70,833	44,093
7	Electricity, Gas & Water	355	25,419	-	-	25,774	9,588
8	Transport & Comm.	343	19,212	-	-	19,555	648
9	Financial Institutions	10,149	65,260	-	-	75,409	3,989
10	Services	12,731	53,843	-	3,571	70,145	23,316
11	Personal	14,530	398,349	-	7,886	420,765	503
12	Agriculture & Allied activities	5	46	-	-	51	6
13	Government	1,358	70,386	-	-	71,744	343
14	Non-resident Lending	-	19,088	-	536	19,624	209
15	All Others	22,557	73,869	-	145	96,571	24,357
16	**Total (1 to 15)**	**102,577**	**873,808**	**3,466**	**88,916**	**1,068,767**	**240,125**

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For the year ended 31 December 2008

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

Sr. No.	Time Band	Overdrafts	Loans	Bills purchased/ discounted	Others	Total	Off balance sheet exp.
		RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
1	Upto 1 month	5,129	57,888	3,420	84,722	151,159	58,776
2	1-3 months	5,129	60,891	46	1,534	67,600	56,347
3	3-6 months	5,129	37,891	-	73	43,093	36,087
4	6-9 months	5,129	37,112	-	29	42,270	20,978
5	9-12 months	5,129	39,483	-	33	44,645	13,110
6	1-3 years	25,644	198,881	-	397	224,922	51,760
7	3-5 years	25,644	146,367	-	18	172,029	1,349
8	Over 5 years	25,644	295,295	-	2,110	323,049	1,718
9	**TOTAL**	**102,577**	**873,808**	**3,466**	**88,916**	**1,068,767**	**240,125**

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

Sr. No.	Economic Sector	Gross loans	Of which NPLs *	General provision held	Specific provision held	Reserve Interest	Provision made during the year	Adv. written-off during year
		RO'000	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
1	Import Trade	81,631	10,198	715	4,301	5,533	4	214
2	Export Trade	193	103	1	37	13	-	-
3	Wholesale & Retail	20,209	10,098	102	4,931	5,088	51	-
4	Mining & Quarrying	35,454	-	355	-	-	-	-
5	Construction	60,809	3,158	577	1,284	841	238	-
6	Manufacturing	70,833	844	700	582	287	9	1
7	Electricity, Gas & Water	25,774	-	258	-	-	-	-
8	Transport & Communications	19,555	2	196	1	1	-	-
9	Financial Institutions	75,409	-	754	-	-	-	-
10	Services	70,145	4,045	661	2,063	1,946	7	-
11	Personal	420,765	9,485	8,771	3,490	4,921	380	45
12	Agriculture & Allied	51	-	1	-	-	-	-
13	Government	71,744	-	718	-	-	-	-
14	Non-resident Lending	19,624	-	196	-	-	-	-
15	All Others	96,571	17	985	5	12	-	-
16	**TOTAL (1 to 15)**	**1,068,767**	**37,950**	**14,990**	**16,694**	**18,642**	**689**	**260**

* Represents only on balance sheet NPLs.

vi) Geographical distribution of amount of impaired loans:

Sr. No.	Countries	Gross loans	Of which NPLs	General provisions held	Specific provisions held	Reserve interest	Provisions made during the year	Advances written- off during year
		RO'000	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
1	Oman	1,049,143	37,950	14,794	16,694	18,642	689	260
2	Other GCC countries	17,919	-	179	-	-	-	-
3	OECD countries*	1,705	-	17	-	-	-	-
4	India	-	-	-	-	-	-	-
5	Pakistan	-	-	-	-	-	-	-
6	Others	-	-	-	-	-	-	-
7	**TOTAL**	**1,068,767**	**37,950**	**14,990**	**16,694**	**18,642**	**689**	**260**

*excluding countries included in row 2

vii) Movement of Gross Loans :

Sr. No.	Details	Movement of Gross Loans during the year					
		Performing Loans		Non-performing Loans			
		Standard	S.M.	Sub-standard	Doubtful	Loss	Total
		RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
1	Opening Balance	680,733	32,898	573	345	35,491	750,040
2	Migration/changes (+/-)	8,632	(10,371)	1,572	73	95	1
3	New Loans	551,589	13,279	268	12	3,314	568,462
4	Recovery Loans	(234,556)	(11,385)	(355)	(64)	(2,741)	(249,101)
5	Loans written-off	(2)				(633)	(635)
6	**Closing Balance**	**1,006,396**	**24,421**	**2,058**	**366**	**35,526**	**1,068,767**
7	Provisions held*	14,990	-	436	117	16,141	31,684
8	Reserve Interest	-	-	473	130	18,039	18,642

*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 Standardised 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.

ii) The Bank is adopting the simplified approach for collateral recognition under the standardised approach, where 0% risk weight is assigned for the exposures

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covered by cash collateral. The total exposure covered by cash collateral, which attracts 0% risk weight is RO 60.08 million. All other credit exposures of Corporate and Retail (except mortgage loans which are assigned 35% risk weight) are assigned 100% risk weight.

iii) Bank also conducts stress tests on portfolio basis at regular intervals to assess the impact of credit risk on its profitability and capital adequacy. The same is placed before the Risk Committee of Board of Directors.

3.3.3 Credit Risk Mitigation: Disclosures for standardised approaches

The Bank has adopted the simple approach for credit risk mitigation and no off-setting 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 endeavours to obtain for it's 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.

As stated above, the Bank has adopted Simple Approach under the Standardised Approach where in the set-off of eligible financial collaterals against the exposures is not considered. The exposures which have been assigned 0% risk weight based on eligible cash collaterals amounts to RO 60.08 million.

Bank is proposing to revise the existing credit risk rating framework in the next year to further strengthen credit risk management. The revised credit risk rating framework shall include more granularity in the rating grades, mapping the single point score provided by the rating model to a scale of 1 to 11 and linking the pricing of the facility to risk rating. 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. The necessary data requirement shall be identified and incorporated in the new core banking system to be implemented. With the availability of the data, a suitable risk based information system shall also be developed. Bank has already started conducting training programmes on risk management practices for the staff and such trainings shall be intensified further to ensure percolation of risk culture across the Bank.

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 and a road map to move to Foundation Internal Rating Based approach (FIRB), for it's approval.

3.3.4 Market Risk

Market Risk is the risk to the Bank's earnings and capital due to changes in the market level of interest 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 categorised into interest rate risk, foreign exchange risk, commodity price risk and equity price risk.

Bank has a comprehensive Treasury Risk Policy which interalia covers 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 Standardised Approach of Basel II.

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

i) Interest Rate Risk:

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). A long-term impact (more than one year) of changing interest rates is on the Bank's networth since the economic value of a bank's assets, liabilities and off-balance sheet positions get affected due to variation in market interest rates.

The responsibility of interest rate risk management rests with the Bank's Asset and Liability Management Committee (ALCO). Bank periodically computes the interest rate risk on the banking book that arises due to re-pricing mismatches in interest rate, sensitive assets and liabilities. For the purpose of monitoring such interest rate risk, the Bank has in place a system that tracks the re-pricing mismatches in interest bearing assets and liabilities. For computation of the interest rate mismatches the guidelines of CBO are followed.

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

Impact on earnings of interest rate risk in the banking book assuming a 100 basis point and 200 basis point parallel

shift in interest rates in RO, USD and other currencies is provided as under:

Impact on earnings **(RO in 000's)**

	+ or - 1%	+ or - 2%
Omani Riyals	1,251	2,502
US Dollars	1,105	2,209
Other currencies	106	212
Total	**2,462**	**4,923**

ii) Foreign Exchange Risk:

Foreign Exchange Risk may be 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 Division of the Bank. 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.

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 the Risk Committee of Board of Directors on a regular basis.

iii) Commodity Risk:

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

iv) 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 division of the Bank. The Bank does not hold trading position in equities. Bank's portfolio is marked to

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For the year ended 31 December 2008

market on a regular basis and the difference in the book value and market value are adjusted against revaluation reserve. Bank also conducts regular stress tests on equity position risk and assesses its impact on profitability and capital adequacy.

v) The Capital Charge:

The capital charge for the entire market risk exposure is computed under the Standardised Approach using the duration method and in accordance with the guidelines issued by CBO in its circular BM 1009. 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 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 capital charge for various components of market risk is presented below :

Type of risk	RO'000 Amount
Interest Rate Risk	7
Equity Position risk	0
Commodities Position Risk	0
Foreign Exchange Position Risk	1,278
TOTAL	**1,285**

For assessing the market risk, the Bank shall, with the approval of CBO, graduate to more advanced measurement techniques from the present Standardised method adopted by the Bank.

3.3.5 Liquidity Risk

Liquidity risk is the potential inability to meet the Bank's 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.

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 for the Bank so as to be always in a position to meet all its maturing liabilities as well as to fund asset growth and business operations. The contingency 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 indicates liquidity gap and 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, Bank monitors the liquidity risk through liquidity ratios, which portrays the liquidity stored in the balance sheet.

The 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. The Bank also prepares projected liquidity report to assess the major liquidity requirement up to one month In advance. Bank has now put in place Asset and Liabilities Management (ALM) software, which can generate liquidity gap report on a daily basis to help management in taking an informed decision to meet liquidity gaps.

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 interalia includes Operational Risk Events, Operational Risk Loss 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.

Basel II has provided three different methods viz., Basic Indicator Approach, Standardised Approach and Advanced Measurement Approach to compute the capital charge of Operational Risk. Bank has adopted the Basic Indicator Approach 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 this approach for capital adequacy calculation purposes, it is the intention of the Bank to move to more advanced approach dividing the Bank's business into eight business lines and assessing the operational risk in each of them. The Bank has put in place a system of collecting and collating data on operational risk events in the Bank as required by the CBO guidelines. The Bank has also initiated the process of implementing best practices for controlling operational risks in various units of the Bank with tools such as Key Risk Indicators and Key Control Standards. The Bank shall review the existing data collection system and strengthen it over a period of time to build a strong loss data base and to move over to the advanced measurement system for Operational Risk with the approval of CBO.

AUDITED FINANCIAL STATEMENTS

Deloitte.

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Independent auditor's report to the shareholders of Bank Dhofar SAOG

Report on the financial statements

We have audited the accompanying financial statements of **Bank Dhofar SAOG**, which comprise of the balance sheet as at 31 December 2008, and the income statement, statement of changes in equity and cash flows statement for the year then ended, and a summary of significant accounting policies and other explanatory notes as set out in pages 67 to 111.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards and the relevant disclosure requirements of the Commercial Companies Law of 1974, as amended and the Rules and Guidelines on disclosure issued by the Capital Market Authority, effective 1 October 2007. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's responsibility

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

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

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

Opinion

In our opinion, the financial statements present fairly, in all material respects the financial position of **Bank Dhofar SAOG** as of 31 December 2008, and of 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 comply, in all material respects, with the relevant disclosure requirements of the Commercial Companies Law of 1974, as amended and the Rules and Guidelines on disclosure issued by the Capital Market Authority, effective 1 October 2007.

Deloitte & Touche

Deloitte & Touche (M.E.)
Muscat, Sultanate of Oman
28 January 2009

Balance sheet

at 31 December 2008

2008 USD'000	2007 USD'000		Notes	2008 RO'000	2007 RO'000
		ASSETS			
301,946	310,203	Cash and cash equivalents	5	116,249	119,428
6,543	6,532	Financial instruments at fair value through profit or loss	6	2,519	2,515
97,626	75,810	Loans and advances to banks	7	37,586	29,187
2,645,301	1,830,242	Loans and advances to customers	8	1,018,441	704,643
35,811	38,078	Available-for-sale investments	9	13,787	14,660
312,904	185,333	Held-to-maturity investments	10	120,468	71,353
10,314	10,314	Intangible asset	11	3,971	3,971
11,940	11,462	Property and equipment	12	4,597	4,413
16,109	12,875	Other assets	13	6,202	4,957
3,438,494	2,480,849	**Total assets**		**1,323,820**	955,127
		LIABILITIES			
232,891	242,841	Due to banks	14	89,663	93,494
2,523,626	1,751,953	Deposits from customers	15	971,596	674,502
92,540	79,925	Other liabilities	16	35,628	30,771
100,000	119,122	Subordinated bonds and loan	17	38,500	45,862
2,949,057	2,193,841	**Total liabilities**		**1,135,387**	844,629
		SHAREHOLDERS' EQUITY			
183,828	137,875	Share capital	18	70,774	53,082
151,964	14,101	Share premium	19	58,506	5,429
37,953	31,555	Legal reserve	20	14,612	12,149
26,668	25,791	Subordinated bonds and loan reserve	20	10,267	9,929
621	9,304	Investment revaluation reserve	20	239	3,582
88,403	68,382	Retained earnings	21	34,035	26,327
489,437	287,008	**Total shareholders' equity**		**188,433**	110,498
3,438,494	2,480,849	**Total liabilities and shareholders' equity**		**1,323,820**	955,127
623,701	435,221	**Contingent liabilities and commitments**	32	**240,125**	167,560
0.69	0.54	**Net assets per share (Rials Omani)**	22	**0.266**	0.208

Eng. Abdul Hafidh Salim Rajab Al-Aujaili
Chairman

Kris Babicci
Chief Executive Officer

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

Income statement

for the year ended 31 December 2008

2008 USD'000	2007 USD'000		Notes	2008 RO'000	2007 RO'000
165,379	134,052	Interest income		63,671	51,610
(61,745)	(55,205)	Interest expense		(23,772)	(21,254)
103,634	78,847	**Net interest income**	23	**39,899**	30,356
13,387	8,870	Fees and commission income		5,154	3,415
(1,657)	(1,203)	Fees and commission expenses		(638)	(463)
11,730	7,667	**Net fees and commission income**		**4,516**	2,952
30,517	27,875	Other income	24	11,749	10,732
145,881	114,389	**Operating income**		**56,164**	44,040
(50,634)	(40,475)	Staff and administrative costs	25	(19,494)	(15,583)
(4,184)	(3,587)	Depreciation	12	(1,611)	(1,381)
(54,818)	(44,062)	**Operating expenses**		**(21,105)**	(16,964)
91,063	70,327	**Profit from operations**		**35,059**	27,076
(14,208)	(8,475)	Provision for loan impairment	8	(5,470)	(3,263)
6,104	3,935	Recoveries from allowance for loan impairment	8	2,350	1,515
(5)	(62)	Bad debts written-off		(2)	(24)
(12,634)	-	Impairment of available-for-sale investments		(4,864)	-
10	132	Financial instruments at fair value through profit or loss		4	51
70,330	65,857	**Profit from operations after provision**		**27,077**	25,355
(8,808)	(6,662)	Income tax expense	27	(3,391)	(2,565)
61,522	59,195	**Profit for the year**		**23,686**	22,790
0.11	0.11	**Earnings per share basic and diluted (Rials Omani)**	28	**0.044**	0.043

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

Statement of changes in equity

for the year ended 31 December 2008

	Notes	Share capital	Share premium	Legal reserve	Subordinated bonds and loan reserve	Investment revaluation reserve	Retained earnings	Total
		RO'000	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
1 January 2007		46,158	5,429	9,870	5,888	2,231	23,705	93,281
Profit for the year		-	-	-	-	-	22,790	22,790
Fair value increase		-	-	-	-	3,932	-	3,932
Net transfer to income statement on sale of available-for-sale investments		-	-	-	-	(2,581)	-	(2,581)
Total recognised income for 2007		-	-	-	-	1,351	22,790	24,141
Dividend paid for 2006		-	-	-	-	-	(6,924)	(6,924)
Bonus issue for 2006		6,924	-	-	-	-	(6,924)	-
Transfer to legal reserve	20	-	-	2,279	-	-	(2,279)	-
Transfer to subordinated bond reserve	20	-	-	-	1,474	-	(1,474)	-
Transfer to subordinated loan reserve	20	-	-	-	2,567	-	(2,567)	-
31 December 2007		53,082	5,429	12,149	9,929	3,582	26,327	110,498

	Notes	Share capital	Share premium	Legal reserve	Subordinated bonds and loan reserve	Investment revaluation reserve	Retained earnings	Total
		USD'000	USD'000	USD'000	USD'000	USD'000	USD'000	USD'000
1 January 2007		119,891	14,101	25,636	15,294	5,795	61,571	242,288
Profit for the year		-	-	-	-	-	59,195	59,195
Fair value increase		-	-	-	-	10,213	-	10,213
Net transfer to income statement on sale of available-for-sale investments		-	-	-	-	(6,704)	-	(6,704)
Total recognised income for 2007		-	-	-	-	3,509	59,195	62,704
Dividend paid for 2006		-	-	-	-	-	(17,984)	(17,984)
Bonus issue for 2006		17,984	-	-	-	-	(17,984)	-
Transfer to legal reserve	20	-	-	5,919	-	-	(5,919)	-
Transfer to subordinated bond reserve	20	-	-	-	3,829	-	(3,829)	-
Transfer to subordinated loan reserve	20	-	-	-	6,668	-	(6,668)	-
31 December 2007		137,875	14,101	31,555	25,791	9,304	68,382	287,008

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

Statement of changes in equity (Continued)

for the year ended 31 December 2008

	Notes	Share capital	Share premium	Legal reserve	Subordinated bonds and loan reserve	Investment revaluation reserve	Retained earnings	Total
		RO'000	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
1 January 2008		53,082	5,429	12,149	9,929	3,582	26,327	110,498
Profit for the year		-	-	-	-	-	23,686	23,686
Fair value decrease		-	-	-	-	(7,108)	-	(7,108)
Net transfer to income statement on sale of available-for-sale investments		-	-	-	-	(1,099)	-	(1,099)
Impairment of available-for-sale investment taken to income statement		-	-	-	-	4,864	-	4,864
Total recognised income for 2008		-	-	-	-	(3,343)	23,686	20,343
Dividend paid for 2007		-	-	-	-	-	(13,271)	(13,271)
Increase in share capital	18	17,692	-	-	-	-	-	17,692
Increase in share premium	19	-	53,077	-	-	-	-	53,077
Increase in legal reserve	20	-	-	94	-	-	-	94
Transfer to legal reserve	20	-	-	2,369	-	-	(2,369)	-
Transferred to retained earnings	20	-	-	-	(7,362)	-	7,362	-
Transfer to subordinated loan reserve	20	-	-	-	7,700	-	(7,700)	-
31 December 2008		70,774	58,506	14,612	10,267	239	34,035	188,433

	Notes	Share capital	Share premium	Legal reserve	Subordinated bonds and loan reserve	Investment revaluation reserve	Retained earnings	Total
		USD'000	USD'000	USD'000	USD'000	USD'000	USD'000	USD'000
1 January 2008		137,875	14,101	31,555	25,791	9,304	68,382	287,008
Profit for the year		-	-	-	-	-	61,522	61,522
Fair value decrease		-	-	-	-	(18,462)	-	(18,462)
Net transfer to income statement on sale of available-for-sale investments		-	-	-	-	(2,855)	-	(2,855)
Impairment of available-for-sale investment taken to income statement		-	-	-	-	12,634	-	12,634
Total recognised income for 2008		-	-	-	-	(8,683)	61,522	52,839
Dividend paid for 2007		-	-	-	-	-	(34,470)	(34,470)
Increase in share capital	18	45,953	-	-	-	-	-	45,953
Increase in share premium	19	-	137,863	-	-	-	-	137,863
Increase in legal reserve	20	-	-	244	-	-	-	244
Transfer to legal reserve	20	-	-	6,154	-	-	(6,154)	-
Transferred to retained earnings	20	-	-	-	(19,123)	-	19,123	-
Transfer to subordinated loan reserve	20	-	-	-	20,000	-	(20,000)	-
31 December 2008		183,828	151,964	37,953	26,668	621	88,403	489,437

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

Cash flows statement

for the year ended 31 December 2008

2008 USD'000	2007 USD'000		2008 RO'000	2007 RO'000
		Cash flows from operating activities		
206,800	167,881	Interest and commission receipts	**79,618**	64,634
(67,060)	(47,382)	Interest payments	**(25,818)**	(18,242)
(42,410)	(41,995)	Cash payments to suppliers and employees	**(16,328)**	(16,168)
97,330	78,504		**37,472**	30,224
		Decrease in operating assets		
(823,161)	(400,197)	Loans and advances to customers	**(316,917)**	(154,076)
(13,829)	5,400	Loans and advances to banks	**(5,324)**	2,079
(127,571)	(185,333)	Purchase of treasury bills and certificates of deposits (net)	**(49,115)**	(71,353)
(964,561)	(580,130)		**(371,356)**	(223,350)
		Increase in operating liabilities		
771,672	460,675	Deposits from customers	**297,094**	177,360
(11,153)	59,268	Due to banks	**(4,294)**	22,818
760,519	519,943		**292,800**	200,178
(106,712)	18,317	**Net cash (used in)/from operating activities**	**(41,084)**	7,052
(6,382)	(4,457)	Income tax paid	**(2,457)**	(1,716)
(113,094)	13,860	**Net cash (used in)/from operating activities**	**(43,541)**	5,336
		Cash flows from investing activities		
301	823	Investment income	**116**	317
(33,868)	(22,177)	Purchase of investments	**(13,039)**	(8,538)
20,294	25,922	Proceeds from sale of investments	**7,813**	9,980
(4,774)	(4,743)	Purchase of property and equipment	**(1,838)**	(1,826)
499	583	Proceeds from sale of property and equipment	**192**	224
(17,548)	407	**Net cash (used in)/from investing activities**	**(6,756)**	157
		Cash flow from financing activities		
184,060	-	Proceeds from rights issue of share capital	**70,863**	-
(19,122)	100,000	Subordinated bonds and loan	**(7,362)**	38,500
(34,470)	(17,984)	Dividend paid	**(13,271)**	(6,924)
130,468	82,016	**Net cash flow from financing activities**	**50,230**	31,576
(174)	96,283	**Net (decrease)/increase in cash and cash equivalents**	**(67)**	37,069
377,132	280,849	Cash and cash equivalents at the beginning of the year	**145,196**	108,127
376,958	377,132	**Cash and cash equivalents at the end of the year**	**145,129**	145,196
301,945	310,203	**Cash and cash equivalents (Note 5)**	**116,249**	119,428
(1,299)	(1,299)	Capital deposit with Central Bank of Oman	**(500)**	(500)
78,496	69,210	Loans and advances to banks due within 90 days	**30,221**	26,646
(2,184)	(982)	Due to banks within 90 days	**(841)**	(378)
376,958	377,132	**Cash and cash equivalents for the purpose of the cash flow statement**	**145,129**	145,196

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

Notes to the financial statements

for the year ended 31 December 2008

1. Legal status and principal activities

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

For the year ended 31 December 2008, the Bank has adopted all of the new and revised standards and interpretations issued by the International Accounting Board (IASB) and the International Financial Reporting Interpretations Committee (IFRIC) of the IASB that are relevant to its operations and effective for periods beginning on 1 January 2008.

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

At the date of authorisation of these financial statements, the following standards and interpretations were in issue but not yet effective:

		Effective for annual periods beginning or after
IFRIC 13:	Customer Loyalty Programmes	1 July 2008
IFRIC 16:	Hedges of a Net Investment in a Foreign Operation	1 October 2008
IFRIC 15:	Agreements for the Construction of Real Estate	1 January 2009
IFRS 1:	(Revised) First-time adoption of International Financial Reporting Standards	1 January 2009
IFRS 2:	(Revised) Share-based Payment	1 January 2009
IFRS 8:	Operating Segments	1 January 2009
IAS 1:	(Revised) Presentation of Financial Statements	1 January 2009
IAS 16:	(Revised) Property, Plant and Equipment	1 January 2009
IAS 19:	(Revised) Employee Benefits	1 January 2009
IAS 20:	(Revised) Government Grants and Disclosure of Government Assistance	1 January 2009
IAS 23:	(Revised) Borrowing Costs	1 January 2009
IAS 29:	(Revised) Financial Reporting in Hyperinflationary Economies	1 January 2009
IAS 32:	(Revised) Financial Instruments : Presentation	1 January 2009
IAS 36:	(Revised) Impairment of Assets	1 January 2009
IAS 38:	(Revised) Intangible Assets	1 January 2009
IAS 40:	(Revised) Investment Property	1 January 2009
IAS 41:	(Revised) Agriculture	1 January 2009
IFRS 3:	(Revised) Business Combinations	1 July 2009
IFRS 5:	(Revised) Non-Current Assets held for Sale and Discontinued Operations	1 July 2009
IAS 27:	(Revised) Consolidated and Separate Financial Statements	1 July 2009
IAS 28:	(Revised) Investment in Associates	1 July 2009
IAS 31:	(Revised) Interests in Joint Ventures	1 July 2009
IAS 39:	(Revised) Financial Instruments: Recognition and Measurement	1 July 2009

The management anticipates that the adoption of the standards will have no material impact on the financial statements of the Bank.

Notes to the financial statements (continued)

for the year ended 31 December 2008

3. Principal accounting policies

3.1. Basis of preparation

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

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 in accordance with IFRS, and the requirements of the commercial companies law of 1974, as amended and disclosure requirements of the Capital Market Authority.

These policies have been consistently applied in dealing with items that are considered material in relation to the Bank's financial statements to all the years presented.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Bank's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in note 4.

3.2. Foreign currency translations

3.2.1. 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.

3.2.2. Transactions and balances

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 income statement. 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.

3.3. Financial instruments

3.3.1. 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.

3.3.1.1. 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.

3. Principal accounting policies (continued)

3.3. Financial instruments (continued)

3.3.1. Classification (continued)

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 income statement.

3.3.1.2. 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.

3.3.1.3. Available-for-sale

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.

3.3.1.4. Held-to-maturity investments

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

3.3.2. Recognition and de-recognition

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.

3.3.3. Measurement

Financial assets are measured initially at cost 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.

3. **Principal accounting policies (continued)**

3.3. Financial instruments (continued)

3.3.3. Measurement (continued)

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.

3.3.4. 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), 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 balance sheet 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 balance sheet date taking into account current market conditions and the current credit worthiness of the counter-parties.

3.3.5. 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 income statement 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 directly in equity, until the financial asset is de-recognised or impaired at which time the cumulative gain or loss previously recognised in equity is recognised in profit or loss.

3.4. 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 from other banks and eligible treasury bills and certificate of deposits.

3.5. 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.

3.6. Offsetting

Financial assets and liabilities are offset and the net amount is reported in the balance sheet 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.

3. **Principal accounting policies (continued)**

3.7. Impairment of financial assets

The Bank assesses at each balance sheet 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 income statement. 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. As a practical expedient, the Bank may measure impairment on the basis of an instrument's fair value using an observable market price.

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.

Notes to the financial statements (continued)

for the year ended 31 December 2008

3. Principal accounting policies (continued)

3.7. Impairment of financial assets (continued)

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 income statement.

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 income statement.

The Bank assesses at each balance sheet 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 equity and recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement. 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 income statement.

3.8. 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
Buildings	7 - 25
Furniture and fixtures	3 - 7
Motor vehicles	3 - 5
Computer equipment	4

3. Principal accounting policies (continued)

3.8. Property and equipment (continued)

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet 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 income statement 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 income statement as an expense when incurred.

3.9. 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.

3.10. Provisions

A provision is recognised in the balance sheet 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.

3.11. Dividends

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

3.12. Interest income and expense

Interest income and expense are recognised in the income statement 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.

3. **Principal accounting policies (continued)**

3.13. 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.

3.14. Taxation

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

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

Deferred income tax is provided in full, using the balance sheet liability method, 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 substantially enacted at the balance sheet 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.

3.15. Employee benefits

End-of-service benefits are accrued in accordance with the terms of employment of the Bank's employees at the balance sheet 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 balance sheet 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 income statement as incurred.

3.16. 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.

3. **Principal accounting policies (continued)**

3.16. Derivative financial instruments (continued)

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 income statement.

3.16.1 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.

3.16.2 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.

3.16.3 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 income statement 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.

3.16.4 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 income statement.

Notes to the financial statements (continued)

for the year ended 31 December 2008

3. Principal accounting policies (continued)

3.16.4 Cash flow hedges (continued)

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 income statement 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.

3.17. 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.

3.18. 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 income statement over the period of the borrowings using the effective interest method.

3.19. 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.

3.20. Fiduciary assets

Assets held in trust or in a fiduciary capacity are not treated as assets of the Bank in the balance sheet.

3.21. 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. Principal accounting policies (continued)

3.22. *Directors' remuneration*

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

4. Critical Accounting Judgement 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 account, or 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.

Held-to-maturity investments

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

(b) Fair value estimation

Fair value is based on quoted market prices at the balance sheet 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 balance sheet date.

(c) Impairment losses on loans and advances

The Bank reviews its loan portfolio to assess impairment at least on a quarterly basis. 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 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 correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. 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.

Notes to the financial statements (Continued)

for the year ended 31 December 2008

4. Critical Accounting Judgement and key sources of estimation uncertainty

(d) 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. The carrying amount of goodwill at the balance sheet date in the financial statements was RO 3,971 (2007 - RO 3,971).

(e) Impairment of available-for-sale investment

The Bank 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.

(f) Depreciation

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.

5. Cash and cash equivalents

	2008 RO'000	2007 RO'000
Cash on hand	**13,114**	8,635
Balances with the Central Bank of Oman	**103,135**	45,793
Certificate of deposits with maturity of 90 days or less	**-**	65,000
	116,249	119,428

At 31 December 2008, cash and cash equivalents included balances with the Central Bank of Oman approximately RO 500,000 (2007 - 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 2007 were issued by the Central Bank of Oman and carried interest rate ranging from 1.90% to 1.98%.

6. Financial instruments at fair value through profit or loss

	2008 RO'000	2007 RO'000
Debts and other fixed income instruments held for trading		
Government Development bonds	**2,519**	2,515

7. Loans and advances to banks

	2008 RO'000	2007 RO'000
Placements with other banks	**30,299**	22,859
Current clearing accounts and bills discounted	**7,287**	6,328
	37,586	29,187

At 31 December 2008, placement with one local bank individually represented 20% or more of the Bank's placements.

At 31 December 2007, no placement with any bank individually represented 20% or more of the Bank's placements.

8. Loans and advances to customers

	2008 RO'000	2007 RO'000
Overdrafts	**102,577**	73,052
Loans	**873,808**	621,846
Loans against trust receipts	**67,791**	38,203
Bills discounted	**3,466**	3,224
Advance against credit cards	**7,945**	4,717
Others	**13,180**	8,998
Gross loans and advances	**1,068,767**	750,040
Less: Impairment allowance	**(50,326)**	(45,397)
Net loans and advances	**1,018,441**	704,643

The movements in the impairment allowance is analysed below:

	2008 RO'000	2007 RO'000
(a) Allowance for loan impairment		
1 January	**28,824**	29,170
Allowance made during the year	**5,470**	3,263
Released to the income statement during the year	**(2,350)**	(1,515)
Written-off during the year	**(260)**	(2,094)
31 December	**31,684**	28,824
(b) Reserved interest		
1 January	**16,573**	16,727
Reserved during the year	**3,544**	3,438
Released to the income statement during the year	**(1,102)**	(824)
Written-off during the year	**(373)**	(2,768)
31 December	**18,642**	16,573
Total impairment allowance	**50,326**	45,397

Notes to the financial statements (Continued)
for the year ended 31 December 2008

8. **Loans and advances to customers (continued)**

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 maximum value through enforcement of collaterals/guarantees of guarantors, etc.

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 2008, out of the total provisions of RO 50,326,142 (2007 – RO 45,397,195) a collective provision made on a general portfolio basis amounting to RO 14,989,548 (2007 - RO 10,208,545).

At 31 December 2008, impaired loans and advances on which interest has been reserved amount to **RO 36,379,850** (2007 - RO 34,893,000) and loans and advances on which interest is not being accrued amount to **RO 1,871,358** (2007 - RO 1,729,189).

Loan and advances are summarised as follows

	2008		2007	
	Loans and advances to customers RO'000	**Loans and advances to banks RO'000**	Loans and advances to customers RO'000	Loans and advances to banks RO'000
Neither past due nor impaired	**1,018,550**	**37,586**	700,585	29,187
Past due but not impaired	**12,267**	**-**	13,046	-
Impaired	**37,950**	**-**	36,409	-
Gross loans and advances	**1,068,767**	**37,586**	750,040	29,187
Less: Impairment allowance	**(50,326)**	**-**	(45,397)	-
Total	**1,018,441**	**37,586**	704,643	29,187

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

	2008 RO'000	2007 RO'000
Past due up to 30 days	**8,458**	8,871
Past due 30 – 60 days	**2,931**	974
Past due 60 – 89 days	**878**	3,201
Totals	**12,267**	13,046

8. **Loans and advances to customers (continued)**

Impaired

	2008 RO'000	2007 RO'000
Substandard	**2,058**	573
Doubtful	**366**	345
Loss	**35,526**	35,491
Total	**37,950**	36,409

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 judgement 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 would otherwise be past due or impaired totalled RO 1,153,000 at 31 December 2008 (2007: RO 1,664,000).

9. **Available-for-sale investments**

	2008 RO'000	2007 RO'000
Equity instruments		
- Quoted	**10,546**	7,552
- Unquoted	**3,241**	7,108
	13,787	14,660

	Cost RO'000	**Fair value 2008 RO'000**	Fair value 2007 RO'000
Quoted on the Muscat Securities Market (by sector)			
Banking and investments	**565**	**558**	1,670
Services	**7,436**	**7,308**	4,640
Industrial	**2,823**	**2,680**	1,242
	10,824	**10,546**	7,552
Unquoted			
Unquoted Omani company	**1,857**	**2,375**	3,937
Unquoted foreign equities	**867**	**866**	3,171
	2,724	**3,241**	7,108
	13,548	**13,787**	14,660

Notes to the financial statements (Continued)

for the year ended 31 December 2008

9. Available-for-sale investments (continued)

At 31 December 2008, the investments are carried at their fair value. The market value in certain cases is higher than the carrying amount. However, the Board of Directors believe that due to the non-liquidity of certain shares, the market value of the quoted securities is not representative of the fair value and hence appropriate adjustments have been made to the market value to reflect the fair value.

10. Held-to-maturity investments

	2008 RO'000	2007 RO'000
Treasury bills above 90 days	**20,468**	36,353
Certificates of deposits above 90 days	**100,000**	35,000
	120,468	71,353

Treasury bills are issued by the commercial banks outside Sultanate of Oman for a term of 3 to 6 months and carry interest rates ranging from 2.61% to 4.34% (2007 - 3.95% to 4.45%).

Outstanding certificate of deposits are issued by the Central Bank of Oman and carry interest rates ranging from 1.25% to 2.2% (2007 – 2.45% to 3.60%).

11. Intangible asset

	2008 RO'000	2007 RO'000
Goodwill	**3,971**	3,971

The goodwill had 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.

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 2007	140	1,573	4,538	760	5,809	73	12,893
Additions	-	-	871	265	588	102	1,826
Disposals	-	-	(142)	(183)	(32)	(110)	(467)
1 January 2008	140	1,573	5,267	842	6,365	65	14,252
Additions	-	-	**978**	**175**	**750**	**(65)**	**1,838**
Disposals	-	-	**(251)**	**(67)**	**(101)**	-	**(419)**
31 December 2008	**140**	**1,573**	**5,994**	**950**	**7,014**	-	**15,671**
Depreciation							
1 January 2007	-	587	3,188	453	4,513	-	8,741
Charge for the year	-	60	534	173	614	-	1,381
Disposals	-	-	(118)	(134)	(31)	-	(283)
1 January 2008	-	647	3,604	492	5,096	-	9,839
Charge for the year	-	**59**	**676**	**192**	**684**	-	**1,611**
Disposals	-	-	**(214)**	**(67)**	**(95)**	-	**(376)**
31 December 2008	-	**706**	**4,066**	**617**	**5,685**	-	**11,074**
Carrying amount							
31 December 2008	**140**	**867**	**1,928**	**333**	**1,329**	-	**4,597**
31 December 2007	140	926	1,663	350	1,269	65	4,413

13. Other assets

	2008 RO'000	2007 RO'000
Interest receivable	**2,207**	2,154
Prepaid expenses	**893**	583
Dividends receivable	**118**	527
Positive fair value of derivatives (note 33)	-	197
Other receivables	**2,984**	1,496
	6,202	4,957

14. Due to banks

	2008 RO'000	2007 RO'000
Syndicated borrowings	**67,375**	67,375
Other borrowings	**19,250**	14,437
Payable on demand	**3,038**	11,682
	89,663	93,494

14. Due to banks (continued)

During previous years, the Bank entered into two mid-term syndicated loan agreements with foreign banks for USD 175,000,000 with three years maturity. The rates of interest are linked to three-month LIBOR subject to competitive margin.

During the current year, the Bank entered into a loan agreement for USD 20,000,000 with a foreign bank having maturity of three years and carries a interest rate linked to three months LIBOR subject to competitive margin.

At 31 December 2007 and 2008, no borrowing from a bank individually represented 20% or more of the Bank's borrowings. The Bank has not had any defaults of principal, interest or other breaches during the year on its borrowed funds (2007 - Nil).

15. Deposits from customers

	2008 RO'000	2007 RO'000
Current accounts	**197,496**	178,137
Savings accounts	**163,853**	142,907
Time deposits	**606,493**	351,393
Margin accounts	**3,754**	2,065
	971,596	674,502

Current accounts and time deposits include deposits from the Government of the Sultanate of Oman and its entities amounting to RO 307,000,000 (2007 - RO 125,797,000).

16. Other liabilities

	2008 RO'000	2007 RO'000
Interest payable	**6,761**	8,807
Creditors and accruals	**24,937**	19,087
Income tax provision	**3,399**	2,523
Deferred tax liability (note 27)	**138**	80
Negative fair value of derivatives (note 33)	**6**	-
Staff terminal benefits	**387**	274
	35,628	30,771

Employee terminal benefits

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

	2008 RO'000	2007 RO'000
1 January	**274**	270
Expense recognised in the income statement	**140**	88
Cash paid to employees	**(27)**	(84)
	387	274

17. Subordinated bonds and loan

	2008 RO'000	2007 RO'000
Subordinated bonds (a)	**-**	7,362
Subordinated loan (b)	**38,500**	38,500
	38,500	45,862

(a) Subordinated bonds

Pursuant to a 'merger agreement' between the Bank and Majan International Bank SAOC (MIB) dated 28 December 2002, on 31 March 2003 the Bank issued 7,361,767 subordinated bonds of RO 1 each with a tenure of 5 years and 1 day to the former shareholders of MIB. These bonds carried a coupon rate of 7% per annum payable annually and were listed at Muscat Security Market. The bonds were matured and repaid in April 2008.

(b) Subordinated loan

In August 2007, the Bank availed an unsecured subordinated loan of USD 100 million with a tenor of 5 years and one month. The rate of interest is linked to three month LIBOR plus margin, payable quarterly, while principal is payable in lumpsum at maturity.

18. Share capital

The authorised share capital consists of 1,000,000,000 shares of RO 0.100 each (2007 - 1,000,000,000 shares of RO 0.100 each).

On 14 October 2008 the Shareholders of the Bank in their Extraordinary General Meeting approved the increase of the share capital of the Bank by issuing a rights issue from RO 53,081,700 to RO 70,773,831. As a result the share capital of the Bank increased to 707,738,306 shares of RO 0.100 each.

At 31 December 2008, the issued and paid-up share capital comprise 707,738,306 shares of RO 0.100 each. (2007 - 530,817,000 shares of RO 0.100 each).

Shareholders

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

	2008		2007	
	No of shares	**%**	No of shares	%
Dhofar International Development and Investment Company SAOG	**218,665,824**	**31**	159,245,096	30
Civil Service Employees' Pension Fund	**70,773,815**	**10**	53,081,689	10
Total	**289,439,639**	**41**	212,326,785	40
Others	**418,298,667**	**59**	318,490,215	60
	707,738,306	**100**	530,817,000	100

Notes to the financial statements (Continued)

for the year ended 31 December 2008

19. Share premium

During the current year, the Bank has issued share of 176,921,306 by way of rights issue at a premium of RO 0.300 representing an increase in share premium by RO 53,076,392. Share premium account is not available for distribution.

20. Reserves

(a) Legal reserve

	2008 RO'000	2007 RO'000
1 January	**12,149**	9,870
Increase due to excess of receipts against rights issue expenses	**94**	-
Appropriation for the year	**2,369**	2,279
31 December	**14,612**	12,149

In accordance with Article 78 of the Commercial Companies Law of 1974, the excess of the receipt of the rights issue expenses transferred to legal reserve.

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 bonds and loan reserves

	2008 RO'000	2007 RO'000
1 January	**9,929**	5,888
Appropriation for the year		
Subordinated bonds reserve	**(7,362)**	1,474
Subordinated loan reserve	**7,700**	2,567
31 December	**10,267**	9,929

Subordinated bonds reserve

Consistent with Bank for International Settlement (BIS) Guidelines on capital adequacy, the Bank transfers an amount equivalent to 20% of the value of the subordinated bonds each year to the subordinated bond reserve until the bonds mature. The bonds matured in April 2008. The amount of the reserve had been transferred to retained earnings through statement of changes in equity upon settlement of the subordinated bonds.

Subordinated loan reserve

Consistent with 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. Since the loan was obtained at the end of August 2007, the Bank transferred 6.67% of the value of the subordinated loan being the period the loan was outstanding in 2007 and 20% in 2008. The amount of the reserve will be transferred to retained earnings through statement of changes in equity upon settlement of the subordinated loan.

20. Reserves (continued)

(c) Investment revaluation reserve

The movements in the investments revaluation reserve is analysed below:

	2008 RO'000	2007 RO'000
1 January	**3,582**	2,231
(Decrease)/increase in fair value	**(7,108)**	3,932
Impairment of available-for-sale investment taken to income statement	**4,864**	-
Net transfer to income statement on sale of available-for-sale investment	**(1,099)**	(2,581)
	239	3,582

21. Retained earnings

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

22. Net assets per share

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

	2008	2007
Net assets (RO)	**188,433,000**	110,498,000
Number of shares outstanding at 31 December (Nos.)	**707,738,306**	530,817,000
Net assets per share (RO)	**0.266**	0.208

23. Net interest income

	2008 RO'000	2007 RO'000
Loans and advances to customers	**60,627**	46,772
Debt investments	**2,358**	3,472
Money market placements	**579**	1,209
Others	**107**	157
Total interest income	**63,671**	51,610
Deposits from customers	**(18,162)**	(15,962)
Money market deposits	**(5,610)**	(5,292)
Total interest expense	**(23,772)**	(21,254)
Net interest income	**39,899**	30,356

Included in interest income from debt investments an amount of RO 2,076,278 (2007: RO 1,913,962) being interest income from held-to-maturity investments.

24. Other income

	2008 RO'000	2007 RO'000
Foreign exchange	**1,512**	1,128
Investment income (a)	**3,789**	4,662
Miscellaneous income	**6,448**	4,942
	11,749	10,732

(a) Investment income

	2008	2007
Dividend income-available-for-sale investments	**1,565**	406
Gain of disposal of available-for-sale investments	**2,108**	3,939
Interest income on financial instruments at fair value through profit or loss	**116**	317
	3,789	4,662

25. Staff and administrative costs

(a) Staff costs

	2008 RO '000	2007 RO'000
Salaries and allowances	**11,030**	7,422
Other personnel costs	**927**	625
Scheme costs - Note (c)	**437**	353
Non-Omani employees terminal benefit - Note (d)	**140**	88
	12,534	8,488

(b) Administrative costs

	2008	2007
Advertising and promotion	**2,116**	2,092
Occupancy costs	**1,532**	1,175
Donation	**-**	1,004
Data processing	**967**	779
Fees and subscriptions	**533**	446
Correspondent charges	**45**	50
Communication costs	**315**	298
Printing and stationery	**281**	219
Professional charges	**358**	373
Insurance	**65**	88
Postage and courier	**69**	61
Vehicle expenses	**148**	104
Travelling expenses	**84**	62
Training costs	**139**	158
Others	**308**	186
	6,960	7,095
	19,494	15,583

At 31 December 2008, the Bank had 840 employees (2007 - 720).

25. Staff and administrative costs (continued)

(c) Oman Social Insurance Scheme (the Scheme)

The Bank contributes to the Scheme for all Omani employees. The Scheme, which is a defined contributions retirement plan, is administered by the Government of Oman. The Bank and Omani employees are required to make monthly contributions to the Scheme based on fixed percentages of basic salaries.

(d) Non-Omani employee terminal benefits

The provision for end-of-service benefits for non-Omani employees is made in accordance with the requirements of the Omani Labour Law. Employees are entitled to benefits based on length of service and final remuneration. Accrued staff terminal benefits are payable on termination of employment.

26. Impairment of financial assets

	2008 RO'000	2007 RO'000
Impairment of available-for-sale investments	**4,864**	-
Provision for loan impairment	**5,470**	3,263
Bad debts written-off	**2**	24
	10,336	3,287
Recoveries from provision for loan impairment	**(2,350)**	(1,515)
Net impairment change of financial assets	**7,986**	1,772

27. Income tax

(a) Income tax expense:

	2008 RO'000	2007 RO'000
Current year tax charge		
Current year	**3,333**	2,517
Under provision of tax in prior year	**-**	96
	3,333	2,613
Deferred tax - Current year	**58**	(48)
	3,391	2,565

27. Income tax (continued)

The Bank is liable to income tax for the year 2008 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:

Current year	2008 RO'000	2007 RO'000
Accounting profit for the year	**27,077**	25,355
Tax expense as provided at the rate above mentioned	**3,246**	3,039
Tax exempt revenue	**(441)**	(468)
Prior year tax	**-**	96
Non-deductible expenses	**586**	(105)
Others	**-**	3
Tax expense	**3,391**	2,565

(b) Temporary timing differences which give rise to deferred tax liabilities are as follows:

	2008 RO'000	2007 RO'000
Depreciation of property and equipment	**101**	82
Intangible assets	**(239)**	(162)
	(138)	(80)

(c) Status of the tax assessments

The Bank's tax assessments for the years 2003 to 2008 have not yet been finalised with the Department of Taxation Affairs at the Ministry of Finance. The Board of Directors believe that additional taxes, if any, in respect of open tax assessments would not be material to the Bank's results and financial position.

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 shareholders as follows:

	2008	2007
Profit for the year (RO)	**23,686,000**	22,790,000
Weighted average number of shares outstanding during the year	**534,210,011**	530,817,000
Earnings per share basic and diluted	**0.044**	0.043

Earnings per share (basic and diluted) has 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.

29. Related parties transactions

In the ordinary course of business, the Bank 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:

	2008 RO'000	2007 RO'000
Loans and advances		
Directors and shareholders holding less than 10% interest in the Bank	**29,096**	21,938
Directors and shareholders holding 10% or more interest in the Bank	**12,608**	13,186
	41,704	35,124
Deposits and other accounts		
Directors and shareholders holding less than 10% interest in the Bank	**62,063**	38,586
Directors and shareholders holding 10% or more interest in the Bank	**89,516**	28,940
	151,579	67,526

	2008 RO'000	2007 RO'000
Contingent liabilities and commitments		
Directors and shareholders holding less than 10% interest in the Bank	**35**	1,308
Directors and shareholders holding 10% or more interest in the Bank	**-**	83
	35	1,391
Remuneration paid to Directors		
Chairman		
- remuneration proposed	**18**	11
- sitting fees paid	**10**	10
Other Directors		
- remuneration proposed	**110**	127
- sitting fees paid	**62**	52
	200	200
Other transactions		
Rental payment to a related party	**180**	59
Other transactions	**27**	22
Key management compensation		
Salaries and other benefits	**612**	373
Other related costs - performance bonus	**305**	185
End-of-service settlement	**432**	-
	1,349	558

Notes to the financial statements (Continued)

for the year ended 31 December 2008

30. Fiduciary assets

	2008 RO'000	2007 RO'000
Funds under management	**604**	86

31. Single borrower and senior members

(a) Single borrower

	2008 RO'000	2007 RO'000
Total exposure:		
Direct	**12,351**	7,883
Indirect (off-balance sheet items)	**-**	-
	12,351	7,883
Number of members	**1**	2

(b) Senior member

	2008	2007
Total exposure:		
Direct	**42,725**	35,775
Indirect	**35**	1,391
	42,760	37,166
Number of members	**22**	23

32. Contingent liabilities and commitments

(a) Credit-related contingent items

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

	2008 RO'000	2007 RO'000
Letters of credit	**76,407**	47,222
Acceptances	**18,116**	14,748
Guarantees and performance bonds	**69,122**	51,955
Advance payment guarantees	**42,211**	28,476
Payment guarantees	**29,398**	23,118
Others	**4,871**	2,041
	240,125	167,560

At 31 December 2008, letters of credit, guarantees and other commitments amounting to RO 2,649,000 (2007 - RO 1,180,000) are counter-guaranteed by other banks.

32. Contingent liabilities and commitments (continued)

(b) Legal cases

During the year 2008, a primary court decided a compensation of RO 5,000,000 to be paid by the Bank to two plaintiffs against their alleged commercial damages. The plaintiffs have appealed requesting increase in the judgement amount. The Bank has also appealed the primary judgment and the Appeal Court has appointed an expert to report on technical issues in the dispute.

The Bank's lawyers believe that grounds of the Bank's appeal are strong and sustainable and anticipated that the Appeal Court would be able to overrule the primary judgement and dismiss the case, taking into consideration that a similar claim from the same plaintiffs against a local bank had been dismissed by a primary court. At this stage of the proceedings, the Bank's lawyers and management believe that it is very difficult to predict the outcome of this litigation.

Also, a plaintiff has filed a lawsuit against the Bank claiming a compensation of RO 1,037,550 for commercial and moral damages. The Bank's lawyers and management believe that the claim has no ground and will be dismissed by the court.

(c) Capital and investment commitments

	2008 RO,000	2007 RO'000
Contractual commitments for property and equipment	**1,117**	860

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.

The notional amounts of certain types of financial instruments provide a basis for comparison with instruments recognised on the balance sheet 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 the Bank'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 2008		Fair value increase/decrease	
	Contract/notional amount RO'000	**Assets RO'000**	**Liabilities RO'000**
Foreign exchange derivatives			
Currency forwards - purchase contracts	**37,814**	**-**	**60**
Currency forwards - sales contracts	**37,843**	**54**	-

33. Derivative financial instruments (continued)

At 31 December 2007

	Contract/notional amount RO'000	Fair value increase Assets RO'000	Fair value increase Liabilities RO'000
Foreign exchange derivatives			
Currency forwards - purchase contracts	62,747	173	-
Currency forwards - sales contracts	62,483	24	-

The following table indicates the periods in which the cash flows associated with derivatives that are expected to impact profit or loss.

	Assets 2008 RO'000	Assets 2007 RO'000	Liabilities 2008 RO'000	Liabilities 2007 RO'000
Expected cash flow less than 6 months	-	197	6	-

34. Fair value information

Based on the valuation methodology outlined below, the fair values of all on and off-balance sheet financial instruments at 31 December 2008 are considered by the Directors 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 balance sheet 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 balance sheet 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.

34. Fair value information (continued)

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 balance sheet date. The estimated fair value of fixed-maturity deposits, including certificates of deposit, is based on discounted cash flows using rates currently offered for deposits of similar remaining maturities. The value of long-term relationships with depositors is not taken into account in estimating fair values.

Other on-balance sheet financial instruments

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

Off-balance sheet financial instruments

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

35. Risk Management

The important types of financial risks to which the Bank is exposed are credit risk, liquidity and market risk. The risk management division of the Bank is an independent and dedicated unit reporting directly to the Risk Committee (RC) 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 Board of Directors 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 Committee of the Board is responsible for reviewing and recommending to the full Board for approval all risk policies and procedures. Risk Committee also reviews the risk profile of the Bank as presented to it by the RMD and appraises the full Board in its periodic meetings.

(i) Credit risk

The most important risk to which the Bank is exposed to is credit risk. To manage the level of credit risk, the Bank deals with counter-parties of good credit standing and when appropriate, obtain collateral.

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.

Notes to the financial statements (Continued)

for the year ended 31 December 2008

35. Risk Management (continued)

(i) Credit risk (continued)

Credit risk is managed by the Risk Management Division 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 analysing 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 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 lending is strictly in accordance with the CBO guidelines. The analysis of credit is given below:

(a) Geographical concentrations

	Assets			Liabilities		
	Loans and Advances to banks	Gross loans and advances	Investment Securities	Deposits from customers	Deposits from banks	Contingent liabilities
	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
31 December 2008						
Sultanate of Oman	**9,625**	**1,049,143**	**115,439**	**966,882**	**2,197**	**135,864**
Other GCC countries	**10,736**	**17,919**	**20,468**	**4,714**	**10,337**	**19,958**
Europe and North America	**17,077**	**1,705**	**570**	**-**	**75,204**	**26,182**
Africa and Asia	**148**	**-**	**297**	**-**	**1,925**	**58,121**
	37,586	**1,068,767**	**136,774**	**971,596**	**89,663**	**240,125**
31 December 2007						
Sultanate of Oman	-	732,599	49,004	669,765	22,854	88,735
Other GCC countries	12,959	17,441	30,589	4,737	1,317	38,190
Europe and North America	14,622	-	8,180	-	67,687	11,478
Africa and Asia	1,606	-	755	-	1,636	29,157
	29,187	750,040	88,528	674,502	93,494	167,560

(b) Customer concentrations

	Assets			Liabilities		
	Loans and Advances to banks	Gross loans and advances	Investment Securities	Deposits from customers	Deposits from banks	Contingent liabilities
	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
31 December 2008						
Personal	**-**	**420,765**	**-**	**318,569**	**-**	**503**
Corporate	**37,586**	**576,258**	**34,255**	**345,991**	**89,663**	**239,279**
Government	**-**	**71,744**	**102,519**	**307,036**	**-**	**343**
	37,586	**1,068,767**	**136,774**	**971,596**	**89,663**	**240,125**
31 December 2007						
Personal	-	275,822	-	267,551	-	1,128
Corporate	29,187	438,241	51,013	281,154	93,494	166,424
Government	-	35,977	37,515	125,797	-	8
	29,187	750,040	88,528	674,502	93,494	167,560

35. Risk Management (continued)

(i) 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 2008			
Personal	**420,765**	**318,569**	**503**
International trade	**81,824**	**17,940**	**40,402**
Construction	**60,809**	**21,892**	**89,058**
Manufacturing	**70,833**	**26,697**	**44,093**
Wholesale and retail trade	**20,209**	**5,044**	**2,949**
Communication and utilities	**45,329**	**11,957**	**10,236**
Financial services	**75,409**	**21,007**	**3,989**
Government	**71,744**	**307,036**	**343**
Other services	**70,145**	**79,009**	**23,316**
Others	**151,700**	**162,445**	**25,236**
	1,068,767	**971,596**	**240,125**

	Assets	Liabilities	
	Gross loans and advances	Deposits from customers	Contingent liabilities
	RO'000	RO'000	RO'000
31 December 2007			
Personal	275,822	267,551	1,128
International trade	103,699	24,107	35,990
Construction	46,594	12,891	58,257
Manufacturing	52,319	12,577	22,251
Wholesale and retail trade	15,565	2,983	2,793
Communication and utilities	35,217	1,323	5,909
Financial services	39,461	15,561	455
Government	35,977	125,797	8
Other services	46,537	58,058	13,417
Others	98,849	153,654	27,352
	750,040	674,502	167,560

35. Risk Management (continued)

(i) Credit risk (continued)

(d) Gross credit exposure:

	Total Gross Exposure		Monthly Average Gross Exposure	
	2008	2007	2008	2007
	RO'000	RO'000	RO'000	RO'000
Overdrafts	102,577	73,052	88,351	68,968
Loans	873,808	621,846	763,481	549,138
Loans against trust receipts	67,791	38,203	57,226	36,583
Bills discounted	3,466	3,224	3,453	2,068
Advance against credit cards	7,945	4,717	6,244	4,268
Others	13,180	8,998	11,688	10,029
Total	1,068,767	750,040	930,443	671,054

(e) Geographical distribution of exposures:

	Sultanate of Oman	Other Countries	Total
	RO'000	RO'000	RO'000
31 December 2008			
Overdrafts	102,577	-	102,577
Loans	854,720	19,088	873,808
Loans against trust receipts	67,255	536	67,791
Bills discounted	3,466	-	3,466
Advance against credit cards	7,945	-	7,945
Others	13,180	-	13,180
	1,049,143	19,624	1,068,767
31 December 2007			
Overdrafts	73,052	-	73,052
Loans	604,471	17,375	621,846
Loans against trust receipts	38,137	66	38,203
Bills discounted	3,224	-	3,224
Advance against credit cards	4,717	-	4,717
Others	8,998	-	8,998
	732,599	17,441	750,040

35. Risk Management (continued)

(i) 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 2008						
Import trade	10,454	40,643	116	30,418	81,631	40,214
Export trade	69	124	-	-	193	188
Wholesale/retail trade	6,108	10,504	-	3,597	20,209	2,949
Mining and quarrying	930	34,195	-	329	35,454	664
Construction	11,219	29,800	-	19,790	60,809	89,058
Manufacturing	11,769	33,070	3,350	22,644	70,833	44,093
Electricity, gas and water	355	25,419	-	-	25,774	9,588
Transport and communication	343	19,212	-	-	19,555	648
Financial institutions	10,149	65,260	-	-	75,409	3,989
Services	12,731	53,843	-	3,571	70,145	23,316
Personal loans	14,530	398,349	-	7,886	420,765	503
Agriculture and allied activities	5	46	-	-	51	6
Government	1,358	70,386	-	-	71,744	343
Non-resident lending	-	19,088	-	536	19,624	209
Others	22,557	73,869	-	145	96,571	24,357
	102,577	873,808	3,466	88,916	1,068,767	240,125
31 December 2007						
Import trade	8,228	72,168	323	15,862	96,581	27,745
Export trade	406	6,688	-	24	7,118	8,245
Wholesale/retail trade	4,185	9,507	10	1,863	15,565	2,793
Mining and quarrying	418	14,173	91	200	14,882	1,954
Construction	10,469	22,411	-	13,714	46,594	58,257
Manufacturing	5,613	30,526	2,660	13,520	52,319	22,251
Electricity, gas and water	462	22,227	-	309	22,998	5,097
Transport and communication	1,239	10,980	-	-	12,219	812
Financial institutions	4,821	34,640	-	-	39,461	455
Services	8,836	35,827	140	1,734	46,537	13,417
Personal loans	12,154	258,976	-	4,692	275,822	1,128
Agriculture and allied activities	-	50	-	-	50	12
Government	1,656	34,321	-	-	35,977	8
Non-resident lending	-	17,441	-	-	17,441	94
Others	14,565	51,911	-	-	66,476	25,292
	73,052	621,846	3,224	51,918	750,040	167,560

Notes to the financial statements (Continued)

for the year ended 31 December 2008

35. Risk Management (continued)

(i) Credit risk (continued)

(g) Residual contractual maturities of the portfolio 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 2008						
Upto 1 month	5,129	57,888	3,420	84,722	151,159	58,776
1 - 3 months	5,129	60,891	46	1,534	67,600	56,347
3 - 6 months	5,129	37,891	-	73	43,093	36,087
6 - 9 months	5,129	37,112	-	29	42,270	20,978
9 - 12 months	5,129	39,483	-	33	44,645	13,110
1 - 3 years	25,644	198,881	-	397	224,922	51,760
3 - 5 years	25,644	146,367	-	18	172,029	1,349
Over 5 years	25,644	295,295	-	2,110	323,049	1,718
	102,577	**873,808**	**3,466**	**88,916**	**1,068,767**	**240,125**
31 December 2007						
Upto 1 month	3,653	84,210	3,115	47,871	138,849	636
1 - 3 months	3,653	34,208	-	1,047	38,908	34,842
3 - 6 months	3,653	50,151	-	216	54,020	30,540
6 - 9 months	3,653	22,763	-	7	26,423	11,975
9 - 12 months	3,653	19,915	-	99	23,667	13,563
1 - 3 years	18,262	143,485	109	383	162,239	52,566
3 – 5 years	18,262	107,534	-	73	125,869	13,724
Over 5 years	18,263	159,580	-	2,222	180,065	9,714
	73,052	621,846	3,224	51,918	750,040	167,560

35. Risk Management (continued)

(i) Credit risk (continued)

(h) Distribution of impaired loans and past due loans by type of Industry:

	Performing loans	Non-performing loans	General provisions held	Specific provisions held	Interest reserve	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 2008							
Import Trade	71,433	10,198	715	4,301	5,533	4	214
Export Trade	90	103	1	37	13	-	-
Wholesale/Retail Trade	10,111	10,098	102	4,931	5,088	51	-
Mining and Quarrying	35,454	-	355	-	-	-	-
Construction	57,651	3,158	577	1,284	841	238	-
Manufacturing	69,989	844	700	582	287	9	1
Electricity, Gas and Water	25,774	-	258	-	-	-	-
Transport and Communication	19,553	2	196	1	1	-	-
Financial Institutions	75,409	-	754	-	-	-	-
Services	66,100	4,045	661	2,063	1,946	7	-
Personal Loans	411,280	9,485	8,771	3,490	4,921	380	45
Agriculture and Allied Activities	51	-	1	-	-	-	-
Government	71,744	-	718	-	-	-	-
Non-Resident Lending	19,624	-	196	-	-	-	-
Others	96,554	17	985	5	12	-	-
	1,030,817	**37,950**	**14,990**	**16,694**	**18,642**	**689**	**260**
31 December 2007							
Import Trade	85,756	10,824	858	5,124	5,074	283	1,231
Export Trade	7,077	42	71	33	9	22	-
Wholesale/Retail Trade	6,469	9,096	65	4,919	4,178	40	5
Mining and Quarrying	14,882	-	149	-	-	47	-
Construction	44,352	2,242	444	1,415	718	142	342
Manufacturing	51,274	1,045	513	722	312	252	290
Electricity, Gas and Water	22,998	-	230	-	-	72	-
Transport and Communication	12,193	26	122	7	2	38	-
Financial Institutions	39,461	-	303	-	-	123	-
Services	42,670	3,867	427	2,126	1,671	179	147
Personal Loans	266,572	9,250	5,741	4,264	4,597	1,801	79
Agriculture and Allied Activities	50	-	1	-	-	1	-
Government	35,977	-	360	-	-	-	-
Non-Resident Lending	17,441	-	174	-	-	54	-
Others	66,459	17	751	5	12	209	-
	713,631	36,409	10,209	18,615	16,573	3,263	2,094

Notes to the financial statements (Continued)

for the year ended 31 December 2008

35. Risk Management (continued)

(i) Credit risk (continued)

(i) Distribution of impaired loans and past due loans by geographical distribution:

	Gross loans RO'000	Non-performing loans RO'000	General provisions held RO'000	Specific provisions held RO'000	Interest reserve RO'000	Provision made during the year RO'000	Advances written-off during the year RO'000
31 December 2008							
Sultanate of Oman	**1,049,143**	**37,950**	**14,794**	**16,694**	**18,642**	**5,448**	**260**
Other Countries	**19,624**	**-**	**196**	**-**	**-**	**22**	**-**
	1,068,767	**37,950**	**14,990**	**16,694**	**18,642**	**5,470**	**260**
31 December 2007							
Sultanate of Oman	732,599	36,409	10,035	18,615	16,573	3,089	2,094
Other Countries	17,441	-	174	-	-	174	-
	750,040	36,409	10,209	18,615	16,573	3,263	2,094

(j) Maximum exposure to credit risk without consideration of collateral held:

	2008 RO' 000	2007 RO' 000
On-Balance sheet items		
Certificate of deposit	**100,000**	100,000
Treasury bills	**20,468**	36,353
Loans and advances to banks	**37,586**	29,187
Loans and advances to customers	**1,018,441**	704,643
Government Development bonds	**2,519**	2,515
	1,179,014	872,698
Off-Balance sheet items		
Financial Guarantees	**140,731**	103,549
	1,319,745	976,247

(ii) Liquidity risk

Liquidity risk arises in the general funding of the Bank's activities and in the management of its positions. It includes both the risk of being unable to fund assets at appropriate maturities and rates and the risk of being unable to liquidate an asset at a reasonable price and in an appropriate time frame.

The Bank's 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 policy also incorporates contingency plans and measures for the Bank so as to be always in a position to meet all its maturing liabilities as well as to fund asset growth and business operations. The contingency 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.

35. Risk Management (continued)

(ii) Liquidity risk (continued)

The Bank monitors it's liquidity risk through internally generated Maturities of Assets and Liabilities (MAL) report which captures all the maturing assets and liabilities into various pre-set time buckets ranging from overnight to five years. The 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. In this, the Bank strictly adheres to the CBO set limit of 15% of cumulative liabilities (outflows) on mismatches in time buckets upto one year. In addition, the Bank sets internal limit on mismatches in time buckets beyond one year which are approved by ALCO. The Bank has in place adequate lines of credit from both local and international banks to meet any unforeseen liquidity requirements.

Maturity profile of assets and liabilities

	Due on demand and up to 30 days RO'000	2 months to 6 months RO'000	7 months to 12 months RO'000	More than 1 year to 5 years RO'000	Over 5 years RO'000	Total RO'000
31 December 2008						
Cash and cash equivalents	**115,749**	**-**	**-**	**-**	**500**	**116,249**
Financial instruments at fair value through profit or loss	**-**	**1,554**	**965**	**-**	**-**	**2,519**
Loans and advances to banks	**30,448**	**3,288**	**-**	**3,850**	**-**	**37,586**
Loans and advances to customers	**151,159**	**110,693**	**74,333**	**396,951**	**285,305**	**1,018,441**
Available-for-sale investments	**-**	**-**	**11,412**	**-**	**2,375**	**13,787**
Held-to-maturity investments	**20,234**	**100,234**	**-**	**-**	**-**	**120,468**
Intangible asset	**-**	**-**	**-**	**-**	**3,971**	**3,971**
Property and equipment	**-**	**-**	**-**	**-**	**4,597**	**4,597**
Other assets	**1,322**	**54**	**14**	**153**	**4,659**	**6,202**
Total assets	**318,912**	**215,823**	**86,724**	**400,954**	**301,407**	**1,323,820**
Due to banks	**12,663**	**38,500**	**1,925**	**36,575**	**-**	**89,663**
Deposits from customers	**215,000**	**332,151**	**179,739**	**154,322**	**90,384**	**971,596**
Other liabilities	**7,418**	**9,398**	**2,976**	**14,209**	**1,627**	**35,628**
Subordinate loan	**-**	**-**	**-**	**38,500**	**-**	**38,500**
Shareholders' equity	**-**	**10,970**	**-**	**-**	**177,463**	**188,433**
Total liabilities and shareholders' equity	**235,081**	**391,019**	**184,640**	**243,606**	**269,474**	**1,323,820**

Notes to the financial statements (Continued)

for the year ended 31 December 2008

35. **Risk Management (continued)**

(ii) **Liquidity risk (continued)**

Maturity profile of assets and liabilities (continued)

	Due on demand and up to 30 days	2 months to 6 months	7 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 2007						
Cash and cash equivalents	118,928	-	-	-	500	119,428
Financial instruments at fair value through profit or loss	-	-	-	2,515	-	2,515
Loans and advances to banks	24,664	4,523	-	-	-	29,187
Loans and advances to customers	138,849	92,929	38,741	288,108	146,016	704,643
Available-for-sale investments	-	-	11,638	-	3,022	14,660
Held-to-maturity investments	5,764	65,589	-	-	-	71,353
Intangible asset	-	-	-	-	3,971	3,971
Property and equipment	-	-	-	-	4,413	4,413
Other assets	1,443	15	77	137	3,285	4,957
Total assets	289,648	163,056	50,456	290,760	161,207	955,127
Due to banks	26,119	-	-	67,375	-	93,494
Deposits from customers	106,377	244,640	145,421	97,757	80,307	674,502
Other liabilities	13,025	5,299	6,090	6,357	-	30,771
Subordinate bonds and loan	-	7,362	-	38,500	-	45,862
Shareholders' equity	-	13,271	-	-	97,227	110,498
Total liabilities and shareholders' equity	145,521	270,572	151,511	209,989	177,534	955,127

(iii) **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. The currency in which the Bank presents its financial statements is Rial Omani, the Bank's financial statements are affected by movements in the exchange rates between U.S Dollar and the 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.

35. **Risk Management (continued)**

(iii) **Market risk (continued)**

(a) **Currency risk (continued)**

The Bank's transactional exposures give rise to foreign currency gains and losses that are recognised in the income statement. 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

	2008	2007
	RO'000	RO'000
Net assets denominated in US Dollars	26,511	20,558
Net assets denominated in other foreign currencies	2,498	3,146
	29,009	23,704

(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 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 Committee of the Board. Impact on earnings of interest rate risk in the banking book is as follows:

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 through various means including monitoring by the Asset Liability Management Committee. Significant changes in gap positions can be made to adjust the profile as market outlooks change.

Notes to the financial statements (Continued)

for the year ended 31 December 2008

35. Risk Management (continued)

(iii) Market risk (continued)

(b) Interest rate risk (continued)

	Effective average interest rate %	Due on demand and within 30 days RO'000	Due within 1 to 6 months RO'000	Due within 7 to 12 months RO'000	Due within 1 to 5 years RO'000	Due after 5 years RO'000	Non-interest bearing RO'000	Total RO'000
31 December 2008								
Cash and cash equivalents	2.0	-	-	-	-	500	115,749	116,249
Financial assets at fair value through profit or loss	4.6	-	1,554	965	-	-	-	2,519
Loans and advances to banks	2.8	30,448	3,288	-	3,850	-	-	37,586
Loans and advances to customers	7.0	242,678	100,435	72,928	362,127	234,344	5,929	1,018,441
Available-for-sale investments		-	-	-	2,375	-	11,412	13,787
Held-to-maturity investments	2.0	20,234	100,234	-	-	-	-	120,468
Intangible asset		-	-	-	-	-	3,971	3,971
Property and equipment		-	-	-	-	-	4,597	4,597
Other assets		-	-	-	-	-	6,202	6,202
Total assets		**293,360**	**205,511**	**73,893**	**368,352**	**234,844**	**147,860**	**1,323,820**
Due to banks	3.3	12,211	75,075	1,925	-	-	452	89,663
Deposits from customers	2.3	267,807	246,642	123,853	72,396	48	260,850	971,596
Other liabilities	-	-	-	-	-	-	35,628	35,628
Subordinate bonds and loan	5.0	-	38,500	-	-	-	-	38,500
Shareholders' equity		-	-	-	-	-	188,433	188,433
Total liabilities and shareholders' equity		**280,018**	**360,217**	**125,778**	**72,396**	**48**	**485,363**	**1,323,820**
On-balance sheet gap		**13,342**	**(154,706)**	**(51,885)**	**295,956**	**234,796**	**(337,503)**	
Cumulative interest sensitivity gap		**13,342**	**(141,364)**	**(193,249)**	**102,707**	**337,503**	**-**	

35. Risk Management (continued)

(iii) Market risk (continued)

(b) Interest rate risk (continued)

	Effective average interest rate %	Due on demand and within 30 days RO'000	Due within 1 to 6 months RO'000	Due within 7 to 12 months RO'000	Due within 1 to 5 years RO'000	Due after 5 years RO'000	Non-interest bearing RO'000	Total RO'000
31 December 2007								
Cash and cash equivalents	3.4	65,000	-	-	-	500	53,928	119,428
Financial assets at fair value through profit or loss		-	-	-	2,515	-	-	2,515
Loans and advances to banks	5.4	24,664	4,523	-	-	-	-	29,187
Loans and advances to customers	7.6	202,671	85,623	31,435	251,584	127,754	5,576	704,643
Available-for-sale investments		-	-	-	3,022	-	11,638	14,660
Held-to-maturity investments	4.7	5,764	65,589	-	-	-	-	71,353
Intangible asset		-	-	-	-	-	3,971	3,971
Property and equipment		-	-	-	-	-	4,413	4,413
Other assets		-	-	-	-	-	4,957	4,957
Total assets		298,099	155,735	31,435	257,121	128,254	84,483	955,127
Due to banks	5.4	25,783	67,375	-	-	-	336	93,494
Deposits from customers	2.7	157,456	168,003	95,503	26,302	48	227,190	674,502
Other liabilities		-	-	-	-	-	30,771	30,771
Subordinate bonds and loan	7.0	-	45,862	-	-	-	-	45,862
Shareholders' equity		-	-	-	-	-	110,498	110,498
Total liabilities and shareholders' equity		183,239	281,240	95,503	26,302	48	368,795	955,127
On-balance sheet gap		114,860	(125,505)	(64,068)	230,819	128,206	(284,312)	
Cumulative interest sensitivity gap		114,860	(10,645)	(74,713)	156,106	284,312	-	

35. Risk Management (continued)

(iii) Market risk (continued)

(b) Interest rate risk (continued)

Impact on earnings due to interest rate risk in the banking book

	+ or – 1%		+ or – 2%	
	2008	2007	**2008**	2007
	RO'000	RO'000	**RO'000**	RO'000
Omani Riyals	**1,251**	2,342	**2,502**	4,685
US Dollars	**1,105**	1,169	**2,209**	2,339
Others Currencies	**106**	90	**212**	180
Total	**2,462**	3,601	**4,923**	7,204

(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 revaluation reserve in shareholder's equity. During the year 2008, equity portfolio eroded in value by RO 7.11 million which has been appropriated against income statement and Revaluation Reserve.

Further, Bank also conducts stress testing and sensitivity analysis to take an informed decision on equity risk exposure.

***If equity price had been 5% lower*:**

If there is adverse impact of 5% on equity portfolio, the value of the portfolio may decrease by RO 674,198/- only (2007: Decrease by RO 732,983/-).

(iv) Operational Risk

The Bank has adopted the Basic Indicator Approach under Basel II for purposes of measuring the 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 risk 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 through the optimisation of the debt and equity balance. The Bank's overall strategy remains unchanged from 2008.

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 capital, share premium, reserves and retained earnings as disclosed in notes 18 to 21.

36. Capital risk management (continued)

Capital adequacy

The ratio of equity to risk weighted assets, as formulated by the Basel II, for the year ended 31 December 2008 is 16.63% (2007 – 14.87%).

Capital structure	**2008**	2007
	RO'000	RO'000
TIER I CAPITAL		
Paid-up capital	**70,774**	53,082
Legal reserve	**14,612**	12,149
Share premium	**58,506**	5,429
Subordinated bonds and loan reserve	**10,267**	9,929
Retained earnings	**19,880**	13,056
Proposed bonus shares	**3,185**	-
Less: Goodwill	**(3,971)**	(3,971)
Less: Negative investment revaluation reserve	**(753)**	-
Total Tier I capital	**172,500**	89,674
TIER II CAPITAL		
Investment revaluation reserve	**442**	1,612
General provision	**14,990**	10,209
Subordinated loan	**23,100**	30,800
Total Tier II capital	**38,532**	42,621
Total eligible capital	**211,032**	132,295
Risk Weighted Assets		
Banking book	**1,167,316**	791,739
Trading book	**16,064**	27,149
Operational risk	**85,899**	70,552
Total	**1,269,279**	889,440
Tier I capital	**172,500**	89,674
Tier II capital	**38,532**	42,621
Tier III capital	**-**	-
Total regulatory capital	**211,032**	132,295
Tier I capital ratio	**13.59%**	10.08%
Total capital ratio	**16.63%**	14.87%

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 balance sheet, 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 2008	**Retail banking RO'000**	**Corporate banking RO'000**	**Treasury and Investments RO'000**	**Total RO'000**
Interest revenues	**28,528**	**32,099**	**3,044**	**63,671**
Segment operating income	**29,221**	**23,272**	**3,671**	**56,164**
Segment assets	**423,946**	**644,821**	**174,360**	**1,243,127**
Less: Impairment allowance				**(50,326)**
				1,192,801
Unallocated assets				**131,019**
Total assets				**1,323,820**
Segment liabilities	**388,638**	**582,958**	**128,163**	**1,099,759**
Unallocated liabilities				**35,628**
Total liabilities				**1,135,387**

37. Segmental information (continued)

At 31 December 2007	Retail banking RO'000	Corporate banking RO'000	Treasury and Investments RO'000	Total RO'000
Interest revenues	21,080	25,692	4,838	51,610
Segment operating income	20,458	17,020	6,562	44,040
Segment assets	280,827	469,213	182,715	932,755
Less: Impairment allowance				(45,397)
				887,358
Unallocated assets				67,769
Total assets				**955,127**
Segment liabilities	277,730	396,772	131,994	806,496
Unallocated liabilities				38,133
Total liabilities				**844,629**

38. Proposed dividend

The Board of Directors in their meeting held on 28 January 2009 proposed a cash dividend of 15.5% for the year ended 31 December 2008 amounting to RO 10.97 million (2007 - RO 13.27 million) and a bonus share issue of 4.5% amounting to 31,848,224 shares (2007 - none) 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 8,543.225 (2007 - RO 7,170) was transferred to the Investor's Trust Fund account as per the guidelines issued by the Capital Market Authority of Oman.

39. Approval of financial statements

The financial statements were approved by the Board of Directors and authorised for issue on 28 January 2009.

40. Comparative figures

Certain amounts of the prior year financial statement have been reclassified to conform with the current year's presentation.