BANK DHOFAR SAOG

Report and financial statements
for the year ended 31 December 2007

BANK DHOFAR SAOG

Report and financial statements for the year ended 31 December 2007

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 2007, and the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes as set out in pages 3 to 57.

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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

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

Opinion

In our opinion, the financial statements present fairly, in all material respects the financial position of **Bank Dhofar SAOG** as of 31 December 2007, 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 (M.E.)
Muscat, Sultanate of Oman
28 January 2008

BANK DHOFAR SAOG

Balance sheet
at 31 December 2007

	Notes	**2007** **RO'000**	2006 RO'000
ASSETS			
Cash and cash equivalents	**3**	**119,428**	84,439
Held-to-maturity investments	**4**	**71,353**	-
Loans and advances to banks	**5**	**29,187**	29,389
Loans and advances to customers	**6**	**704,643**	548,819
Financial instruments at fair value through profit or loss	**7**	**2,515**	9,098
Available-for-sale investments	**8**	**14,660**	10,870
Intangible asset	**9**	**3,971**	3,971
Property and equipment	**10**	**4,413**	4,152
Other assets	**11**	**4,957**	4,061
Total assets		**955,127**	694,799
LIABILITIES			
Due to banks	**12**	**93,494**	70,879
Deposits from customers	**13**	**674,502**	497,142
Other liabilities	**14**	**30,771**	26,135
Subordinated bonds and loan	**15**	**45,862**	7,362
Total liabilities		**844,629**	601,518
SHAREHOLDERS' EQUITY			
Share capital	**16**	**53,082**	46,158
Share premium		**5,429**	5,429
Legal reserve	**17**	**12,149**	9,870
Subordinated bonds and loan reserve	**17**	**9,929**	5,888
Investment revaluation reserve	**17**	**3,582**	2,231
Retained earnings		**26,327**	23,705
Total shareholders' equity		**110,498**	93,281
Total liabilities and shareholders' equity		**955,127**	694,799
Contingent liabilities and commitments	**27**	**167,560**	112,119
Net assets per share (Rials Omani)		**0.208**	0.202

Eng. Abdul Hafidh Salim Rajab Al-Aujaili
Chairman

Ahmed Ali Al Shanfari
Chief Executive Officer

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

Income statement
for the year ended 31 December 2007

	Notes	2007 RO'000	2006 RO'000
Interest income		**51,610**	42,287
Interest expense		**(21,254)**	(16,042)
Net interest income	**20**	**30,356**	26,245
Other income	**21**	**13,684**	8,675
Operating income		**44,040**	34,920
Staff and administrative costs	**22**	**(15,583)**	(12,471)
Depreciation	**10**	**(1,381)**	(1,143)
Operating expenses		**(16,964)**	(13,614)
Profit from operations		**27,076**	21,306
Provision for loan impairment	**6**	**(3,263)**	(2,646)
Recoveries from allowance for loan impairment	**6**	**1,515**	3,517
Bad debts written-off		**(24)**	(158)
Financial instruments at fair value through profit or loss		**51**	(43)
Profit from operations after provision		**25,355**	21,976
Income tax expense	**24**	**(2,565)**	(1,846)
Profit for the year		**22,790**	20,130
Earnings per share basic and diluted (Rials Omani)	**18**	**0.043**	0.038

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

Statement of changes in equity
for the year ended 31 December 2007

	Notes	Share capital RO'000	Share premium RO'000	Legal reserve RO'000	Subordinated bonds and loan reserve RO'000	Investment revaluation reserve RO'000	Retained earnings RO'000	Total RO'000
1 January 2006		41,962	5,429	7,857	4,416	4,289	15,452	79,405
Profit for the year		-	-	-	-	-	20,130	20,130
Fair value decrease		-	-	-	-	(455)	-	(455)
Total recognised income for 2006						(455)	20,130	19,675
Net transfer to income statement on sale of available-for-sale investments		-	-	-	-	(1,603)	-	(1,603)
Dividend paid for 2005		-	-	-	-	-	(4,196)	(4,196)
Bonus issue for 2005		4,196	-	-	-	-	(4,196)	-
Transfer to legal reserve	**17**			2,013			(2,013)	-
Transfer to subordinated bond reserve	**17**	-	-	-	1,472	-	(1,472)	-
31 December 2006		46,158	5,429	9,870	5,888	2,231	23,705	93,281

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

BANK DHOFAR SAOG

Statement of changes in equity
for the year ended 31 December 2007

	Notes	Share capital RO'000	Share premium RO'000	Legal reserve RO'000	Subordinated bonds and loan reserve RO'000	Investment revaluation reserve RO'000	Retained earnings RO'000	Total 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
Total recognised income for 2007		-	-	-	-	3,932	22,790	26,722
Net transfer to income statement on sale of available-for-sale investments		-	-	-	-	(2,581)	-	(2,581)
Dividend paid for 2006		-	-	-	-	-	(6,924)	(6,924)
Bonus issue for 2006		6,924	-	-	-	-	(6,924)	-
Transfer to legal reserve	17	-	-	2,279	-	-	(2,279)	-
Transfer to subordinated bond reserve	17	-	-	-	1,474	-	(1,474)	-
Transfer to subordinated loan reserve	17	-	-	-	2,567	-	(2,567)	-
31 December 2007		**53,082**	**5,429**	**12,149**	**9,929**	**3,582**	**26,327**	**110,498**

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

BANK DHOFAR SAOG

Cash flow statement
for the year ended 31 December 2007

	2007 RO'000	2006 RO'000
Cash flows from operating activities		
Interest and commission receipts	**64,634**	50,030
Interest payments	**(18,242)**	(13,958)
Cash payments to suppliers and employees	**(16,168)**	(5,178)
	30,224	30,894
Increase / (decrease) in operating assets		
Loans and advances to customers	**(154,076)**	(78,753)
Loans and advances to banks	**2,079**	2,086
Purchase of treasury bills and certificates of deposits (net)	**(71,353)**	-
	(223,350)	(76,667)
Increase in operating liabilities		
Deposits from customers	**177,360**	45,010
Due to banks	**22,818**	10,713
	200,178	55,723
Net cash from operating activities	**7,052**	9,950
Income tax paid	**(1,716)**	(1,730)
Net cash generated from operating activities	**5,336**	8,220
Cash flows from investing activities		
Investment income	**317**	498
Purchase of investments	**(8,538)**	(4,066)
Proceeds from sale of investments	**9,980**	6,565
Purchase of property and equipment	**(1,826)**	(1,484)
Proceeds from sale of property and equipment	**224**	101
Net cash generated from investing activities	**157**	1,614
Cash flow from financing activities		
Subordinated loan	**38,500**	-
Dividend paid	**(6,924)**	(4,196)
Net cash flow from / (used in) financing activities	**31,576**	(4,196)
Net increase in cash and cash equivalents	**37,069**	5,638
Cash and cash equivalents at the beginning of the year	**108,127**	102,489
Cash and cash equivalents at the end of the year	**145,196**	108,127
Cash and cash equivalents (Note 3)	**119,428**	84,439
Capital deposit with Central Bank of Oman	**(500)**	(500)
Loans and advances to banks due within 90 days	**26,646**	24,769
Due to banks within 90 days	**(378)**	(581)
Cash and cash equivalents for the purpose of the cash flow statement	**145,196**	108,127

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

1. Legal status and principal activities

Bank Dhofar SAOG (the Bank) is incorporated in the Sultanate of Oman as a public joint stock company and is principally engaged in corporate, retail and investment banking activities. 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. Principal accounting policies

2.1. *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.

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 32.

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

	Effective for annual period beginning or after
IFRIC 11 : IFRS 2: Group and Treasury Share Transactions	1 March 2007
IFRIC 12 : Service Concession Arrangements	1 January 2008
IFRIC 13 : Customer Loyalty Programmes	1 July 2008
IFRIC 14: IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction	1 January 2008
IAS 23 : (Revised) Borrowing Costs	1 January 2009
IFRS 8 : Operating Segments	1 January 2009

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

2. Principal accounting policies (continued)

2.2. *Foreign currency translations*

2.2.1. *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.

2.2.2. *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, such as equities classified as available-for-sale financial assets, are included in the investment revaluation reserve in equity.

2.3. *Financial instruments*

2.3.1. *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.

2.3.1.1. *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.

2.3.1.2. *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.

2.3.1.3. *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.

2. Principal accounting policies (continued)

2.3. *Financial instruments (continued)*

2.3.1.4. *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..

2.3.2. *Recognition and derecognition*

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

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

2.3.3. *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.

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.

2.3.4. *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.

2. Principal accounting policies (continued)

2.3. *Financial instruments (continued)*

2.3.4. *Fair value measurement principles (continued)*

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.

2.3.5. *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 derecognised or impaired at which time the cumulative gain or loss previously recognised in equity is recognised in profit or loss.

2.4. *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.

2.5. *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..

2.6. *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.

2.7. *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:

2. Principal accounting policies (continued)

2.7. *Impairment of financial assets*

(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.

2. Principal accounting policies (continued)

2.7. *Impairment of financial assets (continued)*

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

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

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

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

2. Principal accounting policies (continued)

2.8. *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 instalments over their estimated economic useful lives from the date the asset is brought into use, as follows :

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

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.

2.9. *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.

2.10. *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.

2.11. *Dividends*

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

2. Principal accounting policies (continued)

2.12. *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.

2.13. *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.

2.14. *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.

2. Principal accounting policies (continued)

2.14. *Taxation (continued)*

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.

2.15. *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.

2.16. *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.

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.

2. Principal accounting policies (continued)

2.16. *Derivative financial instruments (continued)*

2.16.1 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.

2.16.2 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.

2.16.3 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.

2.16.4 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.

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.

2. Principal accounting policies (continued)

2.16.4 Cash flow hedges (continued)

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.

2.17. *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.

2.18. *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.

2.19. *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.

2.20. *Directors' remuneration*

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

3. Cash and cash equivalents

	2007 **RO'000**	2006 RO'000
Cash on hand	**8,635**	7,321
Balances with the Central Bank of Oman	**45,793**	14,465
Certificate of deposits	**65,000**	55,000
Treasury bills	**-**	7,653
	119,428	84,439

At 31 December 2007, cash and cash equivalents included balances with the Central Bank of Oman approximately RO 500,000 (2006 - RO 500,000) as minimum reserve requirements. These funds are not available for the Bank's daily business.

4 Held-to-maturity investments

	2007 **RO'000**	2006 RO'000
Treasury bills above 90 days	**36,353**	-
Certificates of deposits above 90 days	**35,000**	-
	71,353	-

5. Loans and advances to banks

	2007 **RO'000**	2006 RO'000
Placements with other banks	**22,859**	27,463
Current clearing accounts & bills discounted	**6,328**	1,926
	29,187	29,389

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

At 31 December 2006, placement with two local banks individually represented 20% or more of the Bank's placements.

6. Loans and advances to customers

	2007 **RO'000**	2006 RO'000
Overdrafts	**73,052**	75,278
Loans	**621,846**	471,091
Loans against trust receipts	**38,203**	33,401
Bills discounted	**3,224**	1,482
Advance against credit cards	**4,717**	4,157
Others	**8,998**	9,307
Gross loans and advances	**750,040**	594,716
Less: Impairment allowance	**(45,397)**	(45,897)
Net loans and advances	**704,643**	548,819

The movement in the impairment allowance is analysed below:

(a) Allowance for loan impairment		
1 January	**29,170**	30,106
Allowance made during the year	**3,263**	2,646
Released to the income statement during the year	**(1,515)**	(3,517)
Written off during the year	**(2,094)**	(65)
31 December	**28,824**	29,170
(b) Reserved interest		
1 January	**16,727**	14,258
Reserved during the year	**3,438**	3,406
Released to the income statement during the year	**(824)**	(476)
Written-off during the year	**(2,768)**	(461)
31 December	**16,573**	16,727
Total impairment allowance	**45,397**	45,897

6. 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 the 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 2007, out of the total provisions of approximately RO **45,397,195** (2006 – RO 45,896,555) provision made on a general portfolio basis for similar assets amounts to approximately RO **10,208,545** (2006 **-** RO 7,516,000).

At 31 December 2007, impaired loans and advances on which interest has been reserved amount to approximately **RO 34,893,000** (2006 - RO 35,285,000) and loans and advances on which interest is not being accrued amount to approximately **RO 1,729,189** (2006 **-** RO 6,338,000).

Loan and advances are summarised as follows

	2007		**2006**	
	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	**700,585**	**29,187**	541,076	29,389
Past due but not impaired	**13,046**	**-**	12,364	-
Impaired	**36,409**	**-**	41,276	-
Gross loans and advances	**750,040**	**29,187**	594,716	29,389
Less: Impairment allowance	**(45,397)**	**-**	(45,897)	-
Total	**704,643**	**29,187**	548,819	29,389

6. Loans and advances to customers (continued)

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 to customers RO'000	Loans and advances to banks RO'000
31 December 2007		
Grade 1	**328,066**	**29,187**
Grade 2	**262,367**	**-**
Grade 3	**90,300**	**-**
Grade 4	**19,852**	**-**
	700,585	**29,187**
31 December 2006		
	RO'000	RO'000
Grade 1	275,808	29,389
Grade 2	166,695	-
Grade 3	80,760	-
Grade 4	17,813	-
	541,076	29,389

Loans and advances past due but not impaired

	2007 RO'000	2006 RO'000
Past due up to 30 days	**8,871**	8,125
Past due 30 – 60 days	**974**	4,177
Past due 60 – 89 days	**3,201**	62
Totals	**13,046**	12,364

Impaired

Substandard	**573**	476
Doubtful	**345**	1,910
Loss	**35,491**	38,890
Total	**36,409**	41,276

6. Loans and advances to customers (continued)

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. Following restructuring, a previously overdue customer account is reset to a normal status and managed together with other similar accounts. Restructuring policies and practices are based on indicators or criteria which, in the judgment of local 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 1,664,000 at 31 December 2007 (2006: RO 1,997,000).

7. Financial instruments at fair value through profit or loss

	Fair value 2007 RO'000	Fair value 2006 RO'000	**Carrying amount 2007 RO'000**	Carrying amount 2006 RO'000
Debts and other fixed income instruments held for trading				
Government Development bonds	**2,515**	9,098	**2,515**	9,098

8. Available-for-sale investments

	2007 RO'000	2006 RO'000
Equity instruments		
- Quoted	**7,552**	7,277
- Unquoted	**7,108**	3,593
	14,660	10,870

8. Available-for-sale investments

		Market value		Carrying amount	
	Cost	**2007**	2006	**2007**	2006
	RO'000	**RO'000**	RO'000	**RO'000**	RO'000
Quoted on the Muscat Securities Market (by sector)					
Investments	**1,335**	**1,670**	2,958	**1,670**	2,958
Insurance	**-**	**-**	727	**-**	727
Services	**3,759**	**4,640**	2,242	**4,640**	2,242
Industrial	**1,071**	**1,442**	1,432	**1,242**	1,350
	6,165	**7,752**	7,359	**7,552**	7,277
Unquoted					
Unquoted Omani company				**3,937**	2,405
Unquoted foreign equities				**3,171**	1,188
				7,108	3,593
				14,660	10,870

At 31 December 2007, 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.

9. Intangible asset

	2007	2006
	RO	RO'000
Goodwill	**3,971**	3,971

Goodwill is carried at cost less accumulated impairment losses and tested annually for impairment.

10. 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 2006	140	1,653	4,039	761	5,119	217	11,929
Additions	-	-	729	131	768	(144)	1,484
Disposals	-	(80)	(230)	(132)	(78)	-	(520)
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)**
31 December 2007	**140**	**1,573**	**5,267**	**842**	**6,365**	**65**	**14,252**
Depreciation							
1 January 2006	-	593	3,021	416	4,052	-	8,082
Charge for the year	-	75	379	151	538	-	1,143
Disposals / written-off	-	(81)	(212)	(114)	(77)	-	(484)
1 January 2007	**-**	**587**	**3,188**	**453**	**4,513**	**-**	**8,741**
Charge for the year	**-**	**60**	**534**	**173**	**614**	**-**	**1,381**
Disposals / written-off	**-**	**-**	**(118)**	**(134)**	**(31)**	**-**	**(283)**
31 December 2007	**-**	**647**	**3,604**	**492**	**5,096**		**9,839**
Carrying amount							
31 December 2007	**140**	**926**	**1,663**	**350**	**1,269**	**65**	**4,413**
31 December 2006	140	986	1,350	307	1,296	73	4,152

Notes to the financial statements
for the year ended 31 December 2007 (continued)

11. Other assets

	2007	2006
	RO'000	RO'000
Interest receivable	**2,154**	1,851
Prepaid expenses	**583**	658
Dividends receivable	**527**	352
Positive fair value of derivatives (note 4)	**197**	81
Other receivables	**1,496**	1,119
	4,957	4,061

12. Due to banks

Syndicated borrowings	**67,375**	67,375
Other borrowings	**14,437**	1,293
Payable on demand	**11,682**	2,211
	93,494	70,879

During the previous year, the Bank entered into a mid-term syndicated loan agreement for US $ 100,000,000 with three years maturity. The lead arrangers for the loan were Dresdner Bank, Natexis Banque and Standard Chartered Bank. This was the second loan the Bank raised from the international market bringing the total international borrowing to US $ 175,000,000 (2006 : US $ 175,000,000). The rates of interest are linked to three month LIBOR subject to competitive margin.

At 31 December 2007 no borrowing from a bank individually represented 20% or more of the Bank's borrowings (2006 – nil). The Bank has not had any defaults of principal, interest or other breaches during the year on its borrowed funds (2006 - Nil).

13. Deposits from customers

	2007	2006
	RO'000	RO'000
Current accounts	**178,137**	123,234
Savings accounts	**142,907**	86,550
Time deposits	**351,393**	285,706
Margin accounts	**2,065**	1,652
	674,502	497,142

Current accounts and time deposits include deposits from the Government of the Sultanate of Oman amounting to RO 125,797,000 (2006 - RO 108,821,000).

14. Other liabilities

	2007 RO'000	2006 RO'000
Interest payable	**8,807**	5,795
Creditors and accruals	**19,087**	12,073
IPO subscriptions	**-**	6,166
Income tax provision	**2,523**	1,626
Deferred tax liability (note 24)	**80**	128
Negative fair value of derivatives (note 4)	**-**	77
Staff terminal benefits	**274**	270
31 December	**30,771**	26,135

Employee terminal benefits

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

	2007 RO'000	2006 RO'000
1 January	**270**	277
Expense recognised in the income statement	**88**	79
Cash paid to employees	**(84)**	(86)
31 December	**274**	270

15. Subordinated bonds and loan

	2007 RO'000	2006 RO'000
Subordinated bonds (a)	**7,362**	7,362
Subordinated loan (b)	**38,500**	-
31 December	**45,862**	7,362

(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 carry a coupon rate of 7% per annum payable annually. The bonds are listed at Muscat Securities Market.

(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 3 month LIBOR plus margin, payable quarterly, while principal is payable in lumpsum at maturity.

16. Share capital

The authorised share capital consists of 1000,000,000 shares of RO 0.100 each (2006 – 1,000,000,000 shares of RO 0.100 each). At 31 December 2007, the issued and paid up share capital comprise 530,817,000 shares of RO 0.100 each. (2006 – 461,579,998 shares of RO 0.100 each)

Shareholders

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

	2007		2006	
	No of shares	**%**	No of shares	%
Dhofar International Development and Investment Company SAOG	**159,245,096**	**30**	138,773,997	30
Civil Service Employees' Pension Fund	**53,081,689**	**10**	46,157,991	10
Total	**212,326,785**	**40**	184,931,988	40
Others	**318,490,215**	**60**	276,648,012	60
	530,817,000	**100**	461,580,000	100

17. Reserves

(a) Legal reserve	**2007**	2006
	RO	RO'000
1 January	**9,870**	7,857
Appropriation for the year	**2,279**	2,013
31 December	**12,149**	9,870

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.

Subordinated bonds and loan reserves

	2007	2006
	RO	RO'000
1 January	**5,888**	4,416
Appropriation for the year		
Subordinated bonds reserve (b)	**1,474**	1,472
Subordinated loan reserve (c)	**2,567**	-
31 December	**9,929**	5,888

17. Reserves (continued)

(b) Subordinated bonds reserve

Consistent with Bank for Interantional 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 are maturing in April 2008. The amount of the reserve will be transferred to retained earnings through statement of changes in equity upon settlement of the subordinated bonds.

(c) Subordinated loan reserve

Consistent with Bank for Interantional 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. The amount of the reserve will be transferred to retained earnings through statement of changes in equity upon settlement of the subordinated loan.

(d) Investment revaluation reserve

	2007 **RO**	2006 RO
1 January	**2,231**	4,289
Increase/ (decrease) in fair value	**3,932**	(455)
Net transfer to income statement on sale of available-for-sale investment	**(2,581)**	(1,603)
31 December	**3,582**	2,231

18. 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:

	2007	2006
Profit for the year (RO)	**22,790,000**	20,130,000
Weighted average number of shares outstanding during the year	**530,817,000**	530,817,000
Earnings per share basic and diluted	**0.043**	0.038

For the purpose of earning per share calculation, the Bank has restated the previous year weighted average number of shares outstanding to include the 15% bonus shares (69,237,000 shares) issued in first quarter of 2007 and par value share is taken is RO 0.100.

19. Capital adequacy

The ratio of equity to risk weighted assets, as formulated by the Basel II, for the year ended 31 December 2007 is **14.87%** (2006 – 13.10%).

Capital structure	**2007**	2006
	RO'000	RO'000
TIER I CAPITAL		
Paid up capital	**53,082**	53,082
Legal reserve	**12,149**	9,870
Share premium	**5,429**	5,429
Subordinated bonds and loan reserve	**9,929**	5,888
Retained earnings	**13,056**	9,857
Less Goodwill	**(3,971)**	(3,971)
Total Tier I capital	**89,674**	80,155
TIER II CAPITAL		
Investment revaluation reserve	**1,612**	1,004
General provision	**10,209**	7,436
Subordinated loan	**30,800**	1,474
Total Tier II capital	**42,621**	9,914
Total eligible capital	**132,295**	90,069
Risk weighted assets		
Banking book	**791,739**	594,854
Trading book	**27,149**	27,822
Operational risk	**70,552**	64,616
Total	**889,440**	687,292
Tier I capital	**89,674**	80,155
Tier II capital	**42,621**	9,914
Tier III capital	**-**	-
Total regulatory capital	**132,295**	90,069
Tier I capital ratio	**10.08%**	11.66%
Total capital ratio	**14.87%**	**13.10%**

20. Net interest income

	2007 RO'000	2006 RO'000
Loans and advances to customers	**46,772**	38,295
Debt investments	**3,472**	1,931
Money market placements	**1,209**	1,946
Others	**157**	115
Total interest income	**51,610**	42,287
Deposits from customers	**(15,962)**	(12,422)
Money market deposits	**(5,292)**	(3,620)
Total interest expense	**(21,254)**	(16,042)
Net interest income	**30,356**	26,245

Included in interest income from debt investments an amount of RO 1,913,962 (2006 : RO 816,599) being interest income from held-to-maturity investments.

21. Other income

	2007 RO'000	2006 RO'000
Fees and commissions (net)	**2,952**	2,159
Foreign exchange	**1,128**	752
Investment income (a)	**4,662**	3,551
Miscellaneous income	**4,942**	2,213
	13,684	8,675

(a) Investment income

	2007 RO'000	2006 RO'000
Dividend income- available-for-sale investments	**406**	1,027
Gain / (loss) of disposal of available-for-sale investments	**3,939**	2,026
Interest income on financial instruments at fair value through profit or loss	**317**	498
	4,662	3,551

The fees and commissions shown above are net of fees and commissions paid of RO 463,000 (2006 - RO 447,000).

22. Staff and administrative costs

(a) Staff costs

	2007 RO '000	2006 RO'000
Salaries and allowances	**7,422**	6,521
Other personnel costs	**625**	589
Scheme costs - Note (b)	**353**	286
Non-Omani employees terminal benefit - Note (c)	**88**	79
	8,488	7,475
Administrative costs		
Advertising and promotion	**2,092**	1,699
Occupancy costs	**1,175**	1,006
Donation	**1,004**	18
Data processing	**779**	601
Fees and subscriptions	**446**	354
Correspondent charges	**50**	36
Communication costs	**298**	238
Printing and stationery	**219**	191
Professional charges	**373**	252
Insurance	**88**	90
Others	**571**	511
	7,095	4,996
	15,583	12,471

At 31 December 2007, the Bank had 720 employees (2006 - 636).

(b) 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.

(c) 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.

23. Impairment of financial assets

	2007 RO'000	2006 RO'000
Financial instruments at fair value through profit or loss	**(51)**	43
Provision for loan impairment	**3,263**	2,646
Bad debts and dues written-off	**24**	158
	3,236	2,847
Recoveries from provision for loan impairment	**(1,515)**	(3,517)
Net impairment change of financial assets	**1,721**	(670)

24. Income tax

(a) Income tax expense:

	2007	2006
Current year tax charge		
Current year	**2,517**	2,194
Under/ (over) provision of tax in prior year	**96**	(444)
	2,613	1,750
Deferred tax expense - Current year	**(48)**	96
	2,565	1,846

The Bank is liable to income tax for the year 2007 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	2007 RO'000	2006 RO'000
Accounting profit for the year	**25,355**	21,976
Tax expense as provided at the rate above mentioned	**3,039**	2,634
Tax exempt revenue	**(468)**	(357)
Prior year tax	**97**	(444)
Deferred tax	**(106)**	-
Others	**3**	13
Tax expense	**2,565**	1,846

24. Income tax (continued)

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

	2007 RO'000	2006 RO'000
Depreciation of property and equipment	**82**	(44)
Intangible assets	**(162)**	(84)
	(80)	(128)

(c) Status of the tax assessments

The Bank's tax assessments for the years 2003 to 2006 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.

25. 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 amount of balances with such related parties are as follows:

	2007 RO'000	2006 RO'000
Loans and advances		
Directors and shareholders holding less than 10% interest in the Bank	**21,938**	21,990
Directors and shareholders holding 10% or more interest in the Bank	**13,186**	6,574
	35,124	28,564
Deposits and other accounts		
Directors and shareholders holding less than 10% interest in the Bank	**38,586**	60,373
Directors and shareholders holding 10% or more interest	**28,940**	15,103
	67,526	75,476

25. Related parties transactions (continued)

	2007 RO'000	2006 RO'000
Contingent liabilities and commitments		
Directors and shareholders holding less than 10% interest in the Bank	**1,308**	806
Directors and shareholders holding 10% or more interest in the Bank	**83**	69
	1,391	875
Remuneration paid to Directors		
Chairman		
– remuneration proposed	**11**	9
– sitting fees paid	**10**	10
Other Directors		
– remuneration proposed	**127**	94
– sitting fees paid	**52**	87
	200	200
Other transactions		
Rental payment to a related party	**59**	42
Other transactions	**22**	20
Key management compensation		
Salaries and other short-term benefits	**373**	634
Other related costs – performance bonus	**185**	251
Dues written off	**-**	134
	558	1,019

26. Single borrower and senior members

(a) Single borrower

	2007 RO'000	2006 RO'000
Total exposure:		
Direct	**7,883**	17,387
Indirect (off-balance sheet items)	**-**	9,740
	7,883	27,127
Number of members	**2**	2

26. Single borrower and senior members (continued)

(b) Senior member

	2007	2006
	RO'000	RO'000
Total exposure:		
Direct	**35,775**	29,112
Indirect	**1,391**	875
	37,166	29,987
Number of members	**23**	11

Excess over limits as specified by the Central Bank of Oman for Single Borrower and Senior Members are secured by cash collaterals, pledge of Government Development Bonds or risk participation arrangements with other commercial banks.

27. Contingent liabilities and commitments

(a) Credit related contingent items

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

	2007	2006
	RO'000	RO'000
Letters of credit	**47,222**	33,520
Acceptances	**14,748**	15,400
Guarantees and performance bonds	**51,955**	27,711
Advance payment guarantees	**28,476**	20,428
Payment guarantees	**23,118**	12,824
Others	**2,041**	2,236
	167,560	112,119

At 31 December 2007, letters of credit, guarantees and other commitments amounting to RO 1,180,000 (2006 -RO 8,844,000) are counter guaranteed by other banks.

(b) Capital and investment commitments

	2007	2006
	RO,000	RO'000
Contractual commitments for property and equipment	**860**	855

(c) Other contingent liabilities and commitments

There are no significant contingencies or commitments which have materialised after the balance sheet date nor are there any acknowledged material claims against the Bank.

28. Analysis of significant assets and liabilities

(a) 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 2007						
Cash and cash Equivalents	**118,928**	**-**	**-**	**-**	**500**	**119,428**
Held-to-maturity investments	**5,764**	**65,589**	**-**	**-**	**-**	**71,353**
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**
Financial instruments at fair value through profit or loss	**-**	**-**	**-**	**2,515**	**-**	**2,515**
Available-for-sale Investments	**-**	**-**	**11,638**	**-**	**3,022**	**14,660**
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**

Notes to the financial statements
for the year ended 31 December 2007 (continued)

28. Analysis of significant assets and liabilities (continued)

(a) Maturity profile of assets and liabilities (continued)

	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 2006						
Cash and cash equivalents	80,113	3,826	-	-	500	84,439
Loans and advances to banks	22,844	6,545	-	-	-	29,389
Loans and advances to customers	95,703	76,995	39,830	242,387	93,904	548,819
Financial instruments at fair value through profit or loss	1,282	-	5,520	2,296	-	9,098
Available-for-sale investments	-	-	8,683	-	2,187	10,870
Intangible asset	-	-	-	-	3,971	3,971
Property and equipment	-	-	-	-	4,152	4,152
Other assets	997	179	15	61	2,809	4,061
Total assets	200,939	87,545	54,048	244,744	107,523	694,799
Due to banks	3,366	-	-	67,513	-	70,879
Deposits from customers	112,801	138,597	105,701	87,549	52,494	497,142
Other liabilities	10,768	6,770	3,037	4,404	1,156	26,135
Subordinate bonds	-	-	-	7,362	-	7,362
Shareholders' equity	-	6,924	-	-	86,357	93,281
Total liabilities and shareholders' equity	126,935	152,291	108,738	166,828	140,007	694,799

Notes to the financial statements
for the year ended 31 December 2007 (continued)

28. Analysis of significant assets and liabilities (continued)

(b) Interest sensitivity gap

Sensitivity to interest rates arises from mismatches in the period to repricing of assets and that of the corresponding liability funding. 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 Committee. Significant changes in gap positions can be made to adjust the profile as market outlooks change.

	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**
Held-to-maturity investments	**4.7**	**5,764**	**65,589**	**-**	**-**	**-**	**-**	**71,353**
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**
Financial assets at fair value through profit or loss		**-**	**-**	**-**	**2,515**	**-**	**-**	**2,515**
Available-for-sale Investments		**-**	**-**	**-**	**3,022**	**-**	**11,638**	**14,660**
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**	**-**	

Notes to the financial statements
for the year ended 31 December 2007 (continued)

28. Analysis of significant assets and liabilities (continued)

(b) Interest sensitivity gap (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 2006								
Cash and cash equivalents	3.7	58,326	3,826	-	-	500	21,787	84,439
Loans and advances to banks	4.9	22,844	1,925	4,620	-	-	-	29,389
Loans and advances to customers	7.8	162,826	69,466	42,648	217,009	52,481	4,389	548,819
Financial assets at fair value through profit or loss	4.3	1,282	-	5,520	2,296	-	-	9,098
Available-for-sale investments		-	-	-	2,187	-	8,683	10,870
Intangible asset		-	-	-	-	-	3,971	3,971
Property and equipment		-	-	-	-	-	4,152	4,152
Other assets		-	-	-	-	-	4,061	4,061
Total assets		245,278	75,217	52,788	221,492	52,981	47,043	694,799
Due to banks	5.4	2,937	67,513	-	-	-	429	70,879
Deposits from customers	2.6	149,664	86,811	72,399	44,275	48	143,945	497,142
Other liabilities	7.0	-	-	-	-	-	26,135	26,135
Subordinate bonds		-	-	-	7,362	-	-	7,362
Shareholders' equity		-	-	-	-	-	93,281	93,281
Total liabilities and shareholders' equity		152,601	154,324	72,399	51,637	48	263,790	694,799
On-balance sheet gap		92,677	(79,107)	(19,611)	169,855	52,933	(216,747)	
Cumulative interest sensitivity gap		92,677	13,570	(6,041)	163,814	216,747	-	

28. Analysis of significant assets and liabilities (continued)

(c) Geographical concentrations

	Assets			Liabilities		
	Loans and Advances to banks RO'000	Gross loans and advances RO'000	Investment Securities RO'000	Deposits from customers RO'000	Deposits from banks RO'000	Contingent liabilities RO'000
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**
31 December 2006						
Sultanate of Oman	14,700	590,385	18,780	492,753	1,768	59,310
Other GCC countries	5,072	4,331	-	4,389	4,892	30,804
Europe and North America	4,997	-	1,188	-	60,754	7,190
Africa and Asia	4,620	-	-	-	3,465	14,815
	29,389	594,716	19,968	497,142	70,879	112,119

(d) Customer concentrations

	Assets			Liabilities		
	Loans and Advances to banks RO'000	Gross loans and advances RO'000	Investment Securities RO'000	Deposits from customers RO'000	Deposits from banks RO'000	Contingent liabilities RO'000
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**
31 December 2006						
Personal	-	229,611	-	169,851	-	524
Corporate	29,389	321,288	10,870	218,470	70,879	111,036
Government	-	43,817	9,098	108,821	-	559
	29,389	594,716	19,968	497,142	70,879	112,119

Notes to the financial statements
for the year ended 31 December 2007 (continued)

28. Analysis of assets and liabilities (continued)

(e) Economic sector concentrations

	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**
31 December 2006			
Personal	229,611	169,851	524
International trade	67,026	29,488	20,974
Construction	48,777	10,979	45,672
Manufacturing	39,349	23,992	21,786
Wholesale and retail trade	14,878	2,161	3,079
Communication and utilities	28,773	1,956	688
Financial services	31,146	18,314	422
Government	43,817	108,821	559
Other services	41,093	64,370	13,150
Others	50,246	67,210	5,265
	594,716	497,142	112,119

29. 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 2007		**Fair value increase**	
	Contract / notional amount RO'000	**Assets RO'000**	**Liabilities RO'000**
Foreign exchange derivatives			
Currency forwards - purchase contracts	**62,747**	**173**	**-**
Currency forwards - sales contracts	**62,483**	**24**	**-**

At 31 December 2006		Fair value increase/ decrease	
	Contract / notional amount RO'000	Assets RO'000	Liabilities RO'000
Foreign exchange derivatives			
Currency forwards - purchase contracts	3,589	-	77
Currency forwards - sales contracts	3,585	81	-

29. Derivative financial instruments (continued)

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

	Assets		Liabilities	
	2007	2006	**2007**	2006
	RO'000	RO'000	**RO'000**	RO'000
Carrying amount				
Expected cash flow				
Less than 6 months	**197**	4	**-**	**-**
6 – 12 months	-	-	-	-
Total	**197**	4	**-**	**-**

30. 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 2007 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 and derivatives

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.

Notes to the financial statements
for the year ended 31 December 2007 (continued)

30. 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

	2007		**2006**	
	Carrying amount RO'000	**Fair value RO'000**	**Carrying amount RO'000**	**Fair value RO'000**
Assets				
Cash and cash equivalents	**119,428**	**119,428**	84,439	84,439
Held-to-maturity investments	**71,353**	**71,353**	-	-
Loans and advances to banks	**29,187**	**29,187**	29,389	29,389
Loans and advances to customers	**704,643**	**704,643**	548,819	548,819
Financial instruments at fair value through profit or loss	**2,515**	**2,515**	9,098	9,098
Available-for-sale investments	**14,660**	**14,660**	10,870	10,870
Other assets	**4,957**	**4,957**	4,061	4,061
Liabilities				
Due to banks	**93,494**	**93,494**	70,879	70,879
Deposits from customers	**674,502**	**674,502**	497,142	497,142
Other liabilities	**30,771**	**30,771**	26,135	26,135
Subordinated bonds and loan	**45,862**	**45,862**	7,362	7,362

31. 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. RC also reviews the risk profile of the bank as presented to it by the RMD and appraises the full Board in it's periodic meetings.

A. 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, obtains 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.

Credit risk is managed by the Risk Management Division through a system of independent risk assessment in credit proposals beyond a threshold limit of OR 100,000 before they are considered by the appropriate approving authorities. The bank has in place a risk grading system for analyzing the risk associated with credit. This facilitates the approving authorities in making their credit decision. In addition RMD assists/ reviews grading of obligors, conducts regular macro analysis of the credit portfolio, and monitors credit concentration limits. Maximum counterparty/group exposures are limited to 15% of the bank's capital base as stipulated by CBO and where a higher limit is required for projects of national importance prior CBO approval is obtained. Individual country limits using 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 are given below:

Notes to the financial statements
for the year ended 31 December 2007 (continued)

31. Risk Management (continued)

Gross credit exposure

	Total Gross Exposure		Monthly average Gross Exposure	
	2007	2006	**2007**	2006
	RO'000	RO'000	**RO'000**	RO'000
Overdrafts	**73,052**	75,278	**68,968**	68,764
Loans	**621,846**	471,091	**549,138**	442,630
Loans against trust receipts	**38,203**	33,401	**36,583**	25,887
Bills discounted	**3,224**	1,482	**2,068**	2,579
Advance against credit cards	**4,717**	4,157	**4,268**	4,136
Others	**8,998**	9,307	**10,029**	8,535
Total	**750,040**	594,716	**671,054**	552,531

Geographical distribution of exposures

	Sultanate of Oman	Gulf Council Countries	Total
	RO'000	**RO'000**	**RO'000**
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**
31 December 2006			
Overdrafts	75,278	-	75,278
Loans	466,760	4,331	471,091
Loans against trust receipts	33,401	-	33,401
Bills discounted	1,482	-	1,482
Advance against credit cards	4,157	-	4,157
Others	9,307	-	9,307
	590,385	4,331	594,716

31. Risk Management (continued)

Industry type distribution of exposures by major types of credit exposures

	Overdrafts RO'000	Loans RO'000	Bills discounted RO'000	Others RO'000	Total RO'000	Off balance sheet exposures RO'000
31 December 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**
31 December 2006						
Import trade	10,532	41,091	494	13,473	65,590	17,547
Export trade	270	1,166	-	-	1,436	5,120
Wholesale/retail trade	4,420	8,869	-	1,589	14,878	3,079
Mining and quarrying	236	10,715	-	305	11,256	384
Construction	10,751	24,502	-	13,524	48,777	46,061
Manufacturing	6,310	21,903	987	10,149	39,349	23,115
Electricity, gas and water	140	16,084	-	247	16,471	29
Transport and communication	311	11,566	-	425	12,302	659
Financial institutions	6,046	24,204	-	-	30,250	422
Services	12,721	25,402	-	2,970	41,093	13,612
Personal loans	19,862	205,620	-	4,129	229,611	524
Agriculture and allied activities	2	52	-	-	54	5
Government	2,086	41,731	-	-	43,817	559
Non resident lending	-	4,331	-	-	4,331	-
Others	1,591	33,855	1	54	35,501	1,003
	75,278	471,091	1,482	46,865	594,716	112,119

Notes to the financial statements for the year ended 31 December 2007 (continued)

31. Risk Management (continued)

Residual contractual maturities of the portfolio by major types of credit exposures

	Overdrafts RO'000	Loans RO'000	Bills discounted RO'000	Others RO'000	Total RO'000	Off balance sheet exposures RO'000
31 December 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**
31 December 2006						
Upto 1 month	3,764	46,944	1,199	43,796	95,703	426
1 - 3 months	3,764	41,307	-	766	45,837	23,314
3 - 6 months	3,764	27,137	173	84	31,158	20,435
6 - 9 months	3,763	21,189	-	-	24,952	8,013
9 - 12 months	3,763	21,460	-	-	25,223	9,075
1 - 3 years	18,820	113,051	110	80	132,061	35,173
3 – 5 years	18,820	114,905	-	334	134,059	9,183
Over 5 years	18,820	85,098	-	1,805	105,723	6,500
	75,278	471,091	1,482	46,865	594,716	112,119

31. Risk Management (continued)

Distribution of impaired loans and past due loans by type of Industry

	Performing loans RO'000	Non performing loans RO'000	General provisions held RO'000	Specific provisions held RO'000	Interest reserve RO'000	Provision made during the year RO'000	Advances written off during the year RO'000
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**
31 December 2006							
Import trade	53,335	12,255	533	5,999	5,611	206	-
Export trade	1,395	41	14	36	5	16	-
Wholesale/retail trade	6,522	8,356	65	4,925	3,431	30	-
Mining and quarrying	11,256	-	113	-	-	-	-
Construction	46,088	2,689	461	1,661	918	1,110	14
Manufacturing	35,290	4,059	353	1,756	743	389	-
Electricity, gas and water	16,471	-	165	-	-	-	-
Transport and communication	12,276	26	123	7	2	6	-
Financial institutions	30,250	-	303	-	-	-	-
Services	36,762	4,331	368	2,259	1,746	9	-
Personal loans	220,107	9,504	4330	5,006	4,261	752	47
Agriculture and allied activities	54	-	1	-	-	-	-
Government	43,817	-	21	-	-	-	-
Non resident lending	4,331	-	43	-	-	-	-
Others	35,486	15	623	5	10	128	4
	553,440	41,276	7,516	21,654	16,727	2,646	65

31. Risk Management (continued)

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 2007							
Sultanate of Oman	**732,599**	**36,409**	**10,035**	**18,615**	**16,573**	**3,089**	**2,094**
Gulf Council Countries	**17,441**	**-**	**174**	**-**	**-**	**174**	**-**
	750,040	**36,409**	**10,209**	**18,615**	**16,573**	**3,263**	**2,094**
31 December 2006							
Sultanate of Oman	590,385	41,276	7,473	21,654	16,727	2,603	65
Gulf Council Countries	4,331	-	43	-	-	43	-
	594,716	41,276	7,516	21,654	16,727	2,646	65

31. Risk Management (continued)

Maximum exposure to credit risk without consideration of collateral held

	2007	2006
On-Balance sheet items	**RO' 000**	RO' 000
Certificate of Deposit	**100,000**	55,000
Treasury bills	**36,353**	7,653
Loans and advances to banks	**29,187**	29,387
Loans and advances to customers	**704,643**	548,819
Government Development Bonds	**2,515**	9,098
	872,698	649,957
Off-Balance sheet items		
Financial Guarantees	**103,549**	60,963
	976,247	710,920

B. 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.

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 make 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.

C. Market risk

Market risk includes currency risk, interest rate risk and price risk.

31. Risk Management (continued)

C. Market risk (continued)

C.1 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.

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 exposure are given below:

Foreign currency exposures

	2007	2006
	RO'000	RO'000
Net assets denominated in US Dollars	**20,558**	3,624
Net assets denominated in other foreign currencies	**3,146**	497
	23,704	4,121

C.2 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 mature at different times or in different amounts. 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:

Impact on earnings of interest rate risk in the banking book

	+ or – 1%		**+ or – 2%**	
	2007	2006	**2007**	2006
	RO'000	RO'000	**RO'000**	RO'000
Omani Riyals	**2,342**	1,975	**4,685**	3,949
US Dollars	**1,169**	786	**2,339**	1,572
Others currencies	**90**	36	**180**	71
Total	**3,601**	2,797	**7,204**	5,592

31. Risk Management (continued)

C.3 Price risks

The Bank is exposed to equity price risks arising from equity investments. Equity investments are held for strategic rather than trading purposes. The Bank does not actively trade these investments.

Equity price sensitivity analysis

The sensitivity analyses below have been determined based on the exposure to equity price risks at the reporting date.

If equity prices had been 5% higher/lower:

Net profit for the year ended 31 December 2007 would have been unaffected as the equity investments are classified as available-for-sale and no investments were impaired; and investment revaluation reserve would increase / decrease by RO 732,983 (2006: increase/decrease by RO 543,521 for the Bank as a result of the changes in fair value of available-for-sale shares.

The Bank's sensitivity to equity prices has not changed significantly from the prior year.

D. 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.

E. 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 2006.

The capital of the Bank consists of debt, which includes borrowings disclosed in note 12, cash and cash equivalents and equity attributable to shareholders of the Bank comprising issued capital, share premium, reserves and retained earnings as disclosed in notes 16 and 17.

32. 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 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**

31. Segmental information (continued)

At 31 December 2006	Retail banking RO'000	Corporate banking RO'000	Treasury and Investments RO'000	Total RO'000
Interest revenues	19,507	18,788	3,992	42,287
Segment Operating Income	17,237	11,941	5,742	34,920
Segment assets	228,370	366,346	112,010	706,726
Less: Impairment allowance				(45,897)
				660,829
Unallocated assets				33,970
Total assets				694,799
Segment liabilities	167,020	330,122	70,879	568,021
Unallocated liabilities				33,497
Total liabilities				601,518

32. Use of estimates

(a) 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.

(b) Impairment of available-for-sale equity instruments

The Bank determines that available-for-sale equity investments are impaired when there has been a significant or prolonged decline in the fair value below its cost. 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.

33. Proposed dividend

The Board of Directors in their meeting held on 28 January 2008 proposed a cash dividend of 25% for the year ended 31 December 2007 amounting to RO 13.27 million (2006 - RO 6.9 million). A resolution to approve these dividends will be presented to the shareholders at the Annual General Meeting.

During the year, unclaimed dividend amounting to RO 7,170 (2006 - RO 2,717) was transferred to the Investor's Trust Fund account as per the guidelines issued by the Capital Market Authority of Oman.

34. Approval of financial statements

The financial statements were approved by the Board of Directors and authorized for issue on 28 January 2008.

35. Comparative figures

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