SOHAR INTERNATIONAL BANK SAOG
(previously Bank Sohar SAOG)

FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2018

Registered office and principal place of business:

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Sultanate of Oman

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PR No. HMH/15/2015; HMA/9/2015

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF SOHAR INTERNATIONAL BANK SAOG (PREVIOUSLY " BANK SOHAR SAOG")

Report on the audit of the financial statements

Opinion

We have audited the financial statements of Sohar International Bank SAOG (the "Bank"), which comprise the statement of financial position as at 31 December 2018, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2018 and its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our report. We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in the Sultanate of Oman, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the financial statements* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying financial statements.

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF
SOHAR INTERNATIONAL BANK SAOG (PREVIOUSLY " BANK SOHAR SAOG") (CONTINUED)

Report on the audit of the financial statements (continued)

Key audit matters (continued)

1. **Impairment provision for loans, advances and financing activities for customers subject to credit risk**

Key audit matters	*How our audit addressed the key audit matters*
At 31 December 2018 the Bank reported gross loans, advances and financing activities for customers amounting to RO 2,340.67 million and RO 88.73 million of expected credit loss allowances. Due to the inherently judgmental nature of the computation of expected credit losses ("ECL") for loans, advances and financing activities for customers, there is a risk that the amount of ECL may be misstated. The key areas of judgement include: • The identification of exposure with a significant deterioration in credit quality. • Assumptions used in the ECL model such as financial condition of counterparty, expected future cash flows, forward looking macroeconomic factors etc. • The need to apply additional overlays to reflect current or future external factors that might not be captured by the expected credit loss model. The accounting policies relating to estimating impairment provision on loans, advances and financing activities for customers, critical accounting estimates and judgements, and the disclosures relating to impairment of loans, advances and financing activities for customers are set out in notes A4.3, A5.1 and B3 to the financial statements.	Our audit procedures in this area included the following: • Evaluated the appropriateness of the Bank's IFRS 9 based impairment provisioning policy and compared it with the requirements of IFRS 9; • We performed audit procedures on the opening balances to gain assurance on the transition. This included evaluating the accounting interpretations for compliance with IFRS 9 and testing the adjustments and disclosures made on transition. • Obtained an understanding of the design and tested the operating effectiveness of relevant controls over ECL model, including model build and approval, ongoing monitoring / validation, model governance and mathematical accuracy. We have also checked completeness and accuracy of the data used and the reasonableness of the management assumptions; • Evaluated Bank's key judgments and estimates made in the ECL computation and involved specialists to assist in evaluating the judgments and estimates relating to probability of default, macro-economic variables and recovery rates; • For a sample of exposures, we performed procedures to evaluate: - Appropriateness of exposure at default, probability of default and loss given default (including collateral values used) in the calculation of ECL; - Timely identification of exposures with a significant increase in credit risk and appropriateness of the Bank's staging; and - ECL calculation. • Checked the completeness of the loans, advances and financing activities for customers (including off balance sheets) in the ECL calculation as of 31 December 2018. We understood the theoretical soundness and tested the mathematical integrity of the models; • Checked the consistency of various inputs and assumptions used by the Bank's management to determine impairment provisions; and • Considered the adequacy of the disclosures in the financial statements in relation to impairment of loans, advances and financing activities for customers and other financial assets subject to credit risk as required under IFRS 9.

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INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF SOHAR INTERNATIONAL BANK SAOG (PREVIOUSLY " BANK SOHAR SAOG") (CONTINUED)

Report on the audit of the financial statements (continued)

Other information included in the Bank's 2018 Annual Report
Those charged with governance and management are responsible for the other information. Other information consists of the information included in the Bank's 2018 Annual Report other than the financial statements and our auditor's report thereon. We obtained the following information prior to the date of our auditor's report, and we expect to obtain the published 2018 Annual Report after the date of our auditor's report:

- Chairman's report
- Corporate governance report
- Management discussion and analysis
- Financial statements of the Islamic Banking Window
- Basel II Pillar III and Basel III Report of the Bank
- Basel II Pillar III and Basel III Report of the Islamic Banking Window

Our opinion on the financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information obtained prior to the date of the auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of management and those charged with governance for the financial statements
Those charged with governance are responsible for the preparation and fair presentation of the financial statements in accordance with IFRS and the relevant requirements of the Commercial Companies Law of 1974, as amended, and the Capital Market Authority ("the CMA") of the Sultanate of Oman, and for such internal control as those charged with governance determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, those charged with governance are responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless those charged with governance either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

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INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF
SOHAR INTERNATIONAL BANK SAOG (PREVIOUSLY " BANK SOHAR SAOG") (CONTINUED)

Report on the audit of the financial statements (continued)

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for expressing an opinion on the effectiveness of the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of those charged with governance's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

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INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF SOHAR INTERNATIONAL BANK SAOG (CONTINUED)

Report on the audit of the financial statements (continued)

Auditor's responsibilities for the audit of the financial statements (continued)

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

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 CMA of the Sultanate of Oman.

Ernst & Young LLC

Philip Stanton
Muscat
12 March 2019

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س.ت: ١٢٢٤٠١٣
ص.ب: ١٧٥٠ روي - ١١٢، سلطنة عمان
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P.O. Box 1750 - P.C. 112, Sultanate of Oman

SOHAR INTERNATIONAL BANK SAOG
(previously Bank Sohar SAOG)

Subject to CBO approval

STATEMENT OF FINANCIAL POSITION
AS AT 31 DECEMBER 2018

31 December 2017 USD'000	31 December 2018 USD'000		Note	31 December 2018 RO'000	31 December 2017 RO'000
		ASSETS			
473,569	**188,197**	Cash and balances with Central Bank	*B1*	**72,456**	182,324
270,657	**315,332**	Due from banks and other money market placements	*B2*	**121,403**	104,203
5,451,294	**5,849,169**	Loans, advances and financing, net	*B3*	**2,251,930**	2,098,748
1,074,652	**1,383,816**	Investment securities	*B4*	**532,769**	413,741
44,439	**51,107**	Property, equipment and fixtures	*B5*	**19,676**	17,109
7,532	**7,532**	Investment properties	*B6*	**2,900**	2,900
61,800	**117,582**	Other assets	*B7*	**45,269**	23,793
7,383,943	**7,912,735**	**TOTAL ASSETS**		**3,046,403**	2,842,818
		LIABILITIES			
1,866,543	**1,875,483**	Due to banks and other money market borrowings	*B8*	**722,061**	718,619
4,267,130	**4,722,995**	Customers' deposits	*B9*	**1,818,353**	1,642,845
81,692	**219,907**	Other liabilities	*B10*	**84,664**	31,451
91,927	**91,927**	Subordinated loans	*B11*	**35,392**	35,392
6,239	**-**	Compulsorily convertible bonds	*B12*	**-**	2,402
48,086	**1,322**	Certificates of deposits	*B13*	**509**	18,513
6,361,617	**6,911,634**	**TOTAL LIABILITIES**		**2,660,979**	2,449,222
		SHAREHOLDERS' EQUITY			
463,545	**514,974**	Share capital	*B14*	**198,265**	178,465
45,732	**46,849**	Share premium	*B14*	**18,037**	17,607
55,683	**63,312**	Legal reserve	*B15*	**24,375**	21,438
2,566	**2,566**	General reserve	*B16*	**988**	988
8,060	**-**	Special reserve	*B17*	**-**	3,103
(1,704)	**(5,517)**	Fair value reserve	*B18*	**(2,124)**	(656)
-	**18,182**	Subordinated loans reserve	*B11*	**7,000**	-
188,704	**100,995**	Retained earnings		**38,883**	72,651
762,586	**741,361**	**TOTAL SHAREHOLDERS' EQUITY**		**285,424**	293,596
259,740	**259,740**	Perpetual Tier 1 capital securities	*B19*	**100,000**	100,000
1,022,326	**1,001,101**	**TOTAL EQUITY**		**385,424**	393,596
7,383,943	**7,912,735**	**TOTAL LIABILITIES AND EQUITY**		**3,046,403**	2,842,818
1,184,683	**1,260,109**	**CONTINGENT LIABILITIES**	*B21.a*	**485,142**	456,103
724,582	**1,141,153**	**COMMITMENTS**	*B21.b*	**439,344**	278,964
Cents	***Cents***			***Baizas***	*Baizas*
42.73	**37.39**	**Net assets per share**	*B20*	**143.96**	164.51

The financial statements were approved and authorised for issue by the Board of Directors on 30 January 2019 and signed on their behalf by:

Chairman

Board member

STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2018

31 December 2017 USD'000	**31 December 2018 USD'000**		Note	**31 December 2018 RO'000**	31 December 2017 RO'000
283,831	**338,501**	Interest income	*C1*	**130,323**	109,275
(159,881)	**(191,356)**	Interest expense	*C2*	**(73,672)**	(61,554)
123,950	**147,145**	**Net interest income**		**56,651**	47,721
9,800	**12,099**	Net income from Islamic financing and investing activities	*C3.b*	**4,658**	3,773
63,912	**86,049**	Other operating income	*C4*	**33,129**	24,606
821	**-**	Net gains on available for sale investments		**-**	316
198,483	**245,293**	**TOTAL OPERATING INCOME**		**94,438**	76,416
(55,023)	**(61,911)**	Staff costs		**(23,836)**	(21,184)
(30,047)	**(35,782)**	Other operating expenses	*C5*	**(13,776)**	(11,568)
(5,314)	**(5,904)**	Depreciation	*B5*	**(2,273)**	(2,046)
(90,384)	**(103,597)**	**TOTAL OPERATING EXPENSES**		**(39,885)**	(34,798)
108,099	**141,696**	**NET OPERATING INCOME BEFORE IMPAIRMENT PROVISIONS**		**54,553**	41,618
-	**(52,268)**	Loan impairment charges and other credit risk provisions (net)	*C6*	**(20,123)**	-
(5,081)	**-**	Impairment on available for sale investments		**-**	(1,956)
(4,532)	**-**	Portfolio impairment allowances	*C6*	**-**	(1,745)
(20,732)	**-**	Specific impairment allowances, net	*C6*	**-**	(7,982)
77,754	**89,428**	**PROFIT BEFORE TAX**		**34,430**	29,935
(11,958)	**(13,153)**	Income tax expense	*C7.a*	**(5,064)**	(4,604)
65,796	**76,275**	**PROFIT FOR THE YEAR**		**29,366**	25,331
		Profit for the year			
63,580	**74,880**	Conventional banking		**28,829**	24,478
2,216	**1,395**	Islamic banking		**537**	853
65,796	**76,275**			**29,366**	25,331
Cents	***Cents***			***Baizas***	*Baizas*
3.32	**2.83**	Basic earnings per share for the year	*C8*	**10.918**	12.776
3.30	**2.83**	Diluted earnings per share for the year	*C8*	**10.918**	12.716

STATEMENT OF COMPREHENSIVE INCOME (continued)
FOR THE YEAR ENDED 31 DECEMBER 2018

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
65,796	**76,275**	**Profit for the year**	**29,366**	25,331
		Other comprehensive income that will not be reclassified to the income statement		
-	**(3,545)**	Revaluation losses on equity instruments held at fair value through other comprehensive income (FVOCI)	**(1,365)**	-
-	**(3,545)**	Total other comprehensive income that will not be reclassified to the income statement	**(1,365)**	
		Other comprehensive income that will be reclassified to the income statement		
		Debt instruments at FVOCI:		
-	**16**	Net changes in allowance for expected credit losses	**6**	-
		Available for sale financial assets:		
301	**-**	Net movement in fair value of available for sale investments, net of income tax	**-**	116
301	**16**	Total other comprehensive income that will be reclassified to the income statement	**6**	116
66,097	**(3,529)**	Total other comprehensive income for the year, net of income tax	**(1,359)**	25,447
66,097	72,746	**Total comprehensive income for the year, net of income tax**	**28,007**	25,447

STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2018
(RO'000)

	Share capital	Share premium	Legal reserve	General reserve	Special reserve	Fair value reserve	Subordinated loans reserve	Retained earnings	Total Shareholders' Equity	Perpetual Tier 1 Capital Securities	Total Equity
Balance as at 1 January 2018	**178,465**	**17,607**	**21,438**	**988**	**3,103**	**(656)**	**-**	**72,651**	**293,596**	**100,000**	**393,596**
Impact of adopting IFRS 9 (Note A6 i)	**-**	**-**	**-**	**-**	**(3,103)**	**(2,018)**	**-**	**(16,713)**	**(21,834)**	**-**	**(21,834)**
Restated opening balance under IFRS 9	**178,465**	**17,607**	**21,438**	**988**	**-**	**(2,674)**	**-**	**55,938**	**271,762**	**100,000**	**371,762**
Total comprehensive income for the year											
Profit for the year	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**29,366**	**29,366**		**29,366**
Other comprehensive income for the year	**-**	**-**	**-**	**-**	**-**	**(1,359)**	**-**	**-**	**(1,359)**	**-**	**(1,359)**
Total comprehensive income for the year	**-**	**-**	**-**	**-**	**-**	**(1,359)**	**-**	**29,366**	**28,007**	**-**	**28,007**
Reclassification of net change in fair value of equity instruments upon derecognition	**-**	**-**	**-**	**-**	**-**	**1,909**	**-**	**(1,909)**	**-**	**-**	**-**
Issue of bonus shares for 2017	**17,846**	**-**	**-**	**-**	**-**	**-**	**-**	**(17,846)**	**-**	**-**	**-**
Conversion of CCB to share capital	**1,954**	**430**	**-**	**-**	**-**	**-**	**-**	**-**	**2,384**	**-**	**2,384**
Dividends paid for 2017	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(8,923)**	**(8,923)**	**-**	**(8,923)**
Additional Tier 1 coupon paid during the year	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(7,750)**	**(7,750)**	**-**	**(7,750)**
Issue expenses - Additional Tier 1 capital	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(56)**	**(56)**	**-**	**(56)**
Transfers (Note B11 & B15)	**-**	**-**	**2,937**	**-**	**-**	**-**	**7,000**	**(9,937)**	**-**	**-**	**-**
Balance as at 31 December 2018	**198,265**	**18,037**	**24,375**	**988**	**-**	**(2,124)**	**7,000**	**38,883**	**285,424**	**100,000**	**385,424**

	Share capital	Share premium	Legal reserve	General reserve	Special reserve	Fair value reserve	Subordinated loans reserve	Retained earnings	Total Shareholders' Equity	Perpetual Tier 1 Capital Securities	Total Equity
Balance as at 1 January 2017	160,450	17,193	18,905	988	-	(772)	50,000	27,122	273,886	-	273,886
Total comprehensive income for the year net of income tax											
Profit for the year	-	-	-	-	-	-	-	25,331	25,331	-	25,331
Other comprehensive income for the year						116			116		116
Total comprehensive income for the year	-	-	-	-	-	116	-	25,331	25,447	-	25,447
Issue of bonus shares for 2016	16,045	-	-	-	-	-	-	(16,045)	-	-	-
Dividends paid for 2016	-	-	-	-	-	-	-	(8,022)	(8,022)	-	(8,022)
Conversion of CCB to share capital	1,970	414	-	-	-	-	-	-	2,384	-	2,384
Issue of Perpetual Tier 1 Capital Securities	-	-	-	-	-	-	-	-	-	100,000	100,000
Issue expenses - Additional Tier 1 capital	-	-	-	-	-	-	-	(99)	(99)	-	(99)
Provision for restructured loans	-	-	-	-	3,103	-	-	(3,103)	-	-	-
Transfers (Note B11 & B15)	-	-	2,533	-	-	-	(50,000)	47,467	-	-	-
Balance as at 31 December 2017	178,465	17,607	21,438	988	3,103	(656)	-	72,651	293,596	100,000	393,596

STATEMENT OF CHANGES IN EQUITY (continued)

FOR THE YEAR ENDED 31 DECEMBER 2018
(USD'000)

	Share capital	Share premium	Legal reserve	General reserve	Special reserve	Fair value reserve	Subordinated loans reserve	Retained earnings	Total Shareholders' Equity	Perpetual Tier 1 Capital Securities	Total Equity
Balance as at 1 January 2018	463,545	45,732	55,683	2,566	8,060	(1,704)	-	188,704	762,586	259,740	1,022,326
Impact of adopting IFRS 9 (Note A6 i)	-	-	-	-	(8,060)	(5,242)	-	(43,410)	(56,712)	-	(56,712)
Restated opening balance under IFRS 9	463,545	45,732	55,683	2,566	-	(6,946)	-	145,294	705,874	259,740	965,614
Total comprehensive income for the year											
Profit for the year	-	-	-	-	-	-	-	76,275	76,275	-	76,275
Other comprehensive income for the year	-	-	-	-	-	(3,529)	-	-	(3,529)	-	(3,529)
Total comprehensive income for the year	-	-	-	-	-	(3,529)	-	76,275	72,746	-	72,746
Reclassification of net change in Fair value of equity instruments upon derecognition	-	-	-	-	-	4,958	-	(4,958)	-	-	-
Issue of bonus shares for 2017	46,353	-	-	-	-	-	-	(46,353)	-	-	-
Conversion of CCB to share capital	5,076	1,117	-	-	-	-	-	-	6,193	-	6,193
Dividends paid for 2017	-	-	-	-	-	-	-	(23,177)	(23,177)	-	(23,177)
Additional Tier 1 coupon	-	-	-	-	-	-	-	(20,130)	(20,130)	-	(20,130)
Issue expenses - Additional Tier 1 capital	-	-	-	-	-	-	-	(145)	(145)	-	(145)
Transfers (Note B11 & B15)	-	-	7,629	-	-	-	18,182	(25,811)	-	-	-
Balance as at 31 December 2018	514,974	46,849	63,312	2,566	-	(5,517)	18,182	100,995	741,361	259,740	1,001,101

	Share capital	Share premium	Legal reserve	General reserve	Special reserve	Fair value reserve	Subordinated loans reserve	Retained earnings	Total Shareholders' Equity	Perpetual Tier 1 Capital Securities	Total Equity
Balance as at 1 January 2017	416,753	44,657	49,104	2,566	-	(2,005)	129,870	70,447	711,392	-	711,392
Total comprehensive income for the year net of income tax											
Profit for the year	-	-	-	-	-	-	-	65,796	65,796	-	65,796
Other comprehensive income for the year	-	-	-	-	-	301	-		301		301
Totalcomprehensive income for the year	-	-	-	-	-	301	-	65,796	66,097	-	66,097
Issue of bonus shares for 2016	41,675	-	-	-	-	-	-	(41,675)	-	-	-
Dividends paid for 2016	-	-	-	-	-	-	-	(20,837)	(20,837)	-	(20,837)
Conversion of CCB to share capital	5,117	1,075	-	-	-	-	-	-	6,192	-	6,192
Issue of Perpetual Tier 1 Capital Securities	-	-	-	-	-	-	-	-	-	259,740	259,740
Additional Tier 1 coupon	-	-	-	-	-	-	-	-	-	-	-
capital	-	-	-	-	-	-	-	(258)	(258)	-	(258)
Reserve for restructured loans	-	-	-	-	8,060	-	-	(8,060)	-	-	-
Transfers (Note B11 & B15)	-	-	6,579	-	-	-	(129,870)	123,291	-	-	-
Balance as at 31 December 2017	463,545	45,732	55,683	2,566	8,060	(1,704)	-	188,704	762,586	259,740	1,022,326

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2018

31 December 2017 USD'000	31 December 2018 USD'000		31 December 2018 RO'000	31 December 2017 RO'000
		OPERATING ACTIVITIES		
77,754	**89,428**	Profit before tax	**34,430**	29,935
		Adjustments for:		
5,314	**5,904**	Depreciation	**2,273**	2,046
25,264	**52,268**	Loan impairment charges and other credit risk provisions, net	**20,123**	9,727
5,081	**5,465**	Net losses on fair value through profit or loss (FVTPL) investments	**2,104**	1,956
(958)	**-**	Gains on sale of available for sale investments	**-**	(369)
2,787	**-**	Provision for withholding tax on overseas interest	**-**	1,073
-	**18**	Loss on sale of fixed assets	**7**	-
(1,592)	**(2,416)**	Income from Islamic investment activities	**(930)**	(613)
(19,574)	**(35,255)**	Interest on investments	**(13,573)**	(7,536)
11,977	**88**	Interest accrued on subordinated loans and compulsorily convertible bonds	**34**	4,611
106,053	**115,501**	**Cash from operating activities before changes in operating assets and liabilities**	**44,468**	40,830
10,761	**42,145**	Due from banks and other money market placements	**16,226**	4,143
(505,218)	**(460,556)**	Loans, advances and financing	**(177,314)**	(194,509)
(130,875)	**33,182**	Investment in held for trading securities	**12,775**	(50,387)
(12,688)	**(56,166)**	Other assets	**(21,624)**	(4,885)
(70,335)	**837,439**	Due to banks and other money market borrowings	**322,414**	(27,079)
288,717	**455,868**	Customers' deposits	**175,509**	111,156
-	**(46,764)**	Certificate of deposits	**(18,004)**	-
(218)	**127,210**	Other liabilities	**48,976**	(84)
(313,803)	**1,047,859**	**Cash from operating activities**	**403,426**	(120,815)
(8,462)	**(10,693)**	Income tax paid	**(4,117)**	(3,258)
(322,265)	**1,037,166**	**Net cash from / (used in) operating activities, net of tax**	**399,309**	(124,073)
		INVESTING ACTIVITIES		
(114,504)	**(183,403)**	Purchase of investments, net	**(70,610)**	(44,084)
54,236	**25,735**	Proceeds from sale/redemption of investments	**9,908**	20,881
(8,912)	**(12,590)**	Acquisition of property, equipment and fixtures	**(4,847)**	(3,431)
-	**1,673**	Income from Islamic investment activities	**644**	-
21,106	**35,255**	Interest received on investments	**13,573**	8,126
(48,074)	**(133,330)**	**Net cash used in investing activities**	**(51,332)**	(18,508)
		FINANCING ACTIVITIES		
(20,836)	**(23,177)**	Dividends paid	**(8,923)**	(8,022)
(15,203)	**(140)**	Interest paid on subordinated loans and compulsorily convertible bonds	**(54)**	(5,853)
(129,870)	**-**	Redemption of subordinated loans	**-**	(50,000)
259,740	**-**	Issue of perpetual Tier 1 capital securities	**-**	100,000
-	**(20,130)**	Interest paid on perpetual Tier 1 capital securities	**(7,750)**	-
(257)	**(145)**	Issue expenses of perpetual Tier 1 capital securities	**(56)**	(99)
93,574	**(43,592)**	**Net cash (used in) / from financing activities**	**(16,783)**	36,026
(276,765)	**860,244**	**NET CHANGE IN CASH AND CASH EQUIVALENTS**	**331,194**	(106,555)
311,872	**35,106**	**CASH AND CASH EQUIVALENT AT BEGINNING OF THE YEAR**	**13,516**	120,071
35,107	**895,350**	**CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR**	**344,710**	13,516
		REPRESENTING:		
472,270	**186,896**	Cash and balances with Central Bank (other than capital deposit) (note B1)	**71,955**	181,824
207,084	**306,935**	Due from banks and other money market placements with OM of 90 days (note B2)	**118,170**	79,727
481,735	**711,992**	Investments securities with original maturity (OM) of 90 days (note B4.b)	**274,117**	185,468
(1,125,982)	**(310,473)**	Due to banks and other money market borrowings with OM of 90 days (note B8)	**(119,532)**	(433,503)
35,107	**895,350**		**344,710**	13,516

A1 Legal status and principal activities

Bank Sohar SAOG ("the Bank") was established in the Sultanate of Oman on 4 March 2007 as a public joint stock company and is primarily engaged in commercial, investment and Islamic banking through a network of thirty commercial banking branches and seven Islamic banking branches within the Sultanate of Oman. The Bank operates under commercial, investment and an Islamic banking licence issued by the Central Bank of Oman (CBO) and is covered by its deposit insurance scheme. The Bank started commercial operations from 9 April 2007. The registered address of the Bank is PO Box 44, Hai Al Mina, Postal Code 114, Muscat, Sultanate of Oman. The Bank has its primary listing on the Muscat Securities Market.

With effect from 30 April 2013, the Bank obtained a license to operate an Islamic Banking Window ("Sohar Islamic"). Sohar Islamic offers a full range of Islamic banking services and products. The principal activities of the window include accepting Shari'a compliant customer deposits, providing Shari'a compliant financing based on Murabaha, Mudaraba, Musharaka, Ijarah, Istisna'a, Salam and providing commercial banking services, investment and other activities permitted under Islamic Banking Regulatory Framework (IBRF).

On 18 December 2018, an extraordinary meeting of the shareholders of Bank Sohar SAOG was held and the shareholders of the bank passed a resolution to amend Section (1) of the Articles of Association of the Bank to change the name of the Bank from 'Bank Sohar SAOG' to 'Sohar International Bank SAOG' (hereinafter referred to as the 'Bank'). This has been confirmed by Ministry of Commerce and Industry on 14 January 2019 by issuing new set of Company documents.

The Bank employed 804 employees as of 31 December 2018 (31 December 2017: 726).

A2 Basis of preparation

A2.1 Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"), relevant requirements of the Commercial Companies Law of Oman of 1974, as amended, Capital Market Authority and the applicable regulations of the CBO.
In accordance with the Royal Decree 69/2012 regarding the amendment in the Banking Law 2000, CBO has issued circular no. IB - 1 under which a complete Islamic Banking Regulatory Framework (IBRF) has been promulgated. The framework identifies the permissible form of trade-related modes of financing including purchase of goods by banks from their customers and immediate resale to them at appropriate profit in price on deferred payment basis. The purchases and sales arising under these arrangements are not reflected in these financial statements as such, but are restricted to the amount of facility actually utilised and the appropriate portion of profit thereon.

The financial results of the Islamic Banking Window have been reflected in these financial statements for reporting purposes after eliminating inter branch transactions / balances. A complete set of standalone financial statements of Sohar Islamic, prepared under AAOIFI, is included in the Bank's annual report.

A2.2 Basis of measurement

The financial statements have been prepared under the historical cost convention except for the following:

- derivative financial instruments are measured at fair value;
- financial instruments classified as trading and at fair value through profit or loss (FVTPL) are measured at fair value;
- available-for-sale financial assets are measured at fair value (before 1 January 2018);
- financial assets at fair value through other comprehensive income (applicable from 1 January 2018);

The statement of financial position is presented in descending order of liquidity as this presentation is more appropriate to the Bank's operations

A2.3 Functional and presentation currency

These financial statements are presented in Rial Omani, which is the Bank's functional currency and also in US Dollars, for the convenience of readers. The US Dollar amounts, which are presented in these financial statements have been translated from the Rial Omani amounts at an exchange rate of US Dollar 1 = RO 0.385 and RO 1 = 1000 baizas. All financial information presented in Rial Omani and US Dollars has been rounded to the nearest thousands, unless otherwise indicated.

A2.4 Use of estimates and judgements

In preparation of the Bank's financial statements, management requires to make certain estimates and assumptions that affect the reported amount of financial assets and liabilities and the resultant allowances for impairment and fair values. In particular, considerable judgment by management is required in the estimation of the amount and timing of future cash flows when determining the level of allowances required for impaired loans and receivables as well as allowances for impairment provision for unquoted investment securities. Estimates and judgments are continually evaluated and are based on historical experience and other factors including expectations of future events that are believed to be reasonable under the circumstances. Actual results may differ from these estimates.

A2 Basis of preparation (continued)

A2.4 Use of estimates and judgements (continued)

The estimates and underlying assumptions are reviewed on a regular basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods. Estimates considered by the Bank to have a significant risk of material adjustment in subsequent periods are discussed in note A5.

A3 Changes in accounting policies and disclosures

A3.1 Standards, amendments and interpretations effective in 2018 and relevant for the Bank's operations

For the year ended 31 December 2018, the Bank has adopted all of the following new and revised standards and interpretations issued by the International Accounting Standards Board (IASB) and the International Financial Reporting Interpretations Committee (IFRIC) of the IASB that are relevant to its operations and effective for periods beginning on 1 January 2018.

- IFRS 9 Financial Instruments
- IFRS 15 Revenue from Contracts with Customers
- IFRIC 22 Foreign Currency Transactions and Advance Consideration

The adoption of the above did not result in any changes to previously reported net profit or equity of the Bank except as mentioned below.

A3.1.a IFRS 9 Financial Instruments

IFRS 9 has significant impact on the Bank's financial statements and details are set out below:

The Bank has adopted IFRS 9 as issued by the IASB in July 2014 with a date of transition of 1 January 2018, which resulted in changes in accounting policies and adjustments to the amounts previously recognised in the financial statements. The Bank did not early adopt IFRS 9 in any previous periods.

As permitted by the transitional provisions of IFRS 9, the Bank elected not to restate comparative figures. Any adjustments to the carrying amounts of financial assets and liabilities at the date of transition were recognised in the opening retained earnings and other reserves of the current year. Consequently, for notes disclosures, the consequential amendments to IFRS 7 disclosures have been applied only to the current year. The comparative year notes disclosures repeat those disclosures made in the prior year.

The adoption of IFRS 9 has resulted in changes in the Bank's accounting policies for recognition, classification and measurement of financial assets and financial liabilities and impairment of financial assets. IFRS 9 also significantly amends other standards dealing with financial instruments such as IFRS 7 'Financial Instruments: Disclosures'.

The key changes to the Bank's accounting policies resulting from its adoption of IFRS 9 are summarised below.

Classification of financial assets and financial liabilities
IFRS 9 contains three principal classification categories for financial assets: measured at amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL). IFRS 9 classification of financial assets is generally based on the business model in which a financial asset is managed and its contractual cash flows. The standard eliminates the existing IAS 39 categories of held-to-maturity, loans and receivables and available-for-sale. Under IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of the standard are never bifurcated. Instead, the whole hybrid instrument is assessed for classification.

IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities. However, although under IAS 39 all fair value changes of liabilities designated under the fair value option were recognised in profit or loss, under IFRS 9 fair value changes are generally presented as follows:

- the amount of change in the fair value that is attributable to changes in the credit risk of the liability is presented in OCI; and
- the remaining amount of change in the fair value is presented in profit or loss.

A3 Changes in accounting policies and disclosures (continued)

A3.1 Standards, amendments and interpretations effective in 2018 and relevant for the Bank's operations (continued)

A3.1.a IFRS 9 Financial Instruments (continued)

Impairment of financial assets
IFRS 9 replaces the 'incurred loss' model in IAS 39 with an 'expected credit loss' model. The new impairment model also applies to certain loan commitments and financial guarantee contracts but not to equity investments.

Hedge accounting
IFRS 9 introduced a new hedge accounting model to simplify hedge accounting outcomes and provide a better linkage between an entity's risk management strategy, the rationale for hedging and the impact of hedging on the financial statements. Some of the key improvements in the standard impacting the Bank include:

1. Hedge effectiveness – IFRS 9 standard requires that the hedge effectiveness assessment be forward-looking and does not prescribe defined effectiveness parameters. Under IAS 39, an entity had to test effectiveness both retrospectively and prospectively subject to 80 to 125 percent effectiveness requirement.
2. Hedge discontinuation. IFRS 9 standard provides that discontinuation of hedge accounting will only happen under specified circumstances. Under IAS 39, the Bank may revoke the hedging relationship if it seems fit.

These changes have not had a material impact on the statement of comprehensive income of the Bank. In addition, some of the basics of hedge accounting applicable to the Bank under IAS 39 do not change as a result of IFRS 9 adoption.

Transition
Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively, except as described below:

- Comparative periods have not been restated. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 are recognised in retained earnings and reserves as at 1 January 2018. Accordingly, the information presented for 2017 does not reflect the requirements of IFRS 9 and therefore is not comparable to the information presented for 2018 under IFRS 9.

- The following assessments have been made on the basis of the facts and circumstances that existed at the date of initial application.
  - The determination of the business model within which a financial asset is held.
  - The designation and revocation of previous designations of certain financial assets as measured at FVTPL

The CBO has issued guidelines relating to implementation of IFRS 9. The relevant requirements relating to transition are set out below:

- Should the existing loan loss impairment computed in accordance with the requirements of IAS 39 and CBO guidelines be higher than the impairment allowance computed under IFRS 9, the related difference (net of tax) be transferred to a loan loss impairment reserve from retained earnings as of 1 January 2018.
- In the subsequent years, where the allowance for loan loss impairment computed in accordance with CBO requirements is higher than the allowance for loan loss impairment loss computed under IFRS 9, the difference (net of tax) should be transferred to the aforementioned loan loss impairment reserve from retained earnings.
  The related impairment reserve will not be available for dividend distribution or for inclusion in the regulatory capital. Any subsequent utilisation of the impairment reserve would require prior approval of the CBO.

Refer A6 for impact on adoption of IFRS 9

A3.1.b IFRS 7 Financial Instruments Disclosures

To reflect the differences between IFRS 9 and IAS 39, IFRS 7 Financial Instruments: Disclosures was updated and the Bank has adopted it, together with IFRS 9, for the year beginning 1 January 2018. Changes include transition disclosures as shown in Note A6 and detailed qualitative and quantitative information about the ECL calculations such as the assumptions and inputs used are set out in Note A5.1.

A3 Changes in accounting policies and disclosures (continued)

A3.1 Standards, amendments and interpretations effective in 2018 and relevant for the Bank's operations (continued)

A3.1.c IFRS 15 - Revenue from Contracts with Customers

This standard on revenue recognition replaces IAS 11, 'Construction contracts', and IAS 18,'Revenue' and related interpretations.

IFRS 15 is more prescriptive, provides detailed guidance on revenue recognition and reduces the use of judgment in applying revenue recognition policies and practices as compared to the replaced IFRS and related interpretations.

Revenue is recognised when a customer obtains control of a good or service. A customer obtains control when it has the ability to direct the use of and obtain the benefits from the good or service.

The Bank also operates a rewards programme which allows customers to accumulate points when they purchase products on the Bank's credit cards. The points can then be redeemed for shopping rewards, cash back or air miles, subject to a minimum number of points being obtained.

The core principle of IFRS 15 is that an entity recognises revenue as it transfers the promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.

IFRS 15 also includes a comprehensive set of disclosure requirements that will result in an entity providing users of financial statements with comprehensive information about the nature, amount, timing and uncertainty of revenue and cash flows arising from the entity's contracts with customers.

The Bank has assessed that the impact of IFRS 15 is not material on the financial statements of the Bank as at the adoption date and the reporting date.

A3.2 Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Bank:

IFRS 16 – Leases
The IASB issued IFRS 16 Leases (IFRS 16), which requires lessees to recognise assets and liabilities for most leases. The standard includes two recognition exemptions for lessees – leases of 'low-value' assets (e.g., personal computers) and short-term leases (i.e., leases with a lease term of 12 months or less). For lessors, there is little change to the existing accounting in IAS 17 Leases. The Bank will perform a detailed assessment in the future to determine the extent. The new standard will be effective for annual periods beginning on or after 1 January 2019. IFRS 16 also requires lessees and lessors to make more extensive disclosures than under IAS 17. The Bank is in the process of assessing the impact of above standard. Based on the initial assessment, the above standard has no material impact on the financial statements of the Bank as at the reporting date.

Other standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Bank:

- IFRIC Interpretation 23 Uncertainty over Income Tax Treatment
- Annual Improvements 2015 - 2017 cycle (issued in 2017)
    - IAS 23 Borrowing Costs

A4 Significant accounting policies

The accounting policies set out below have been applied consistently by the Bank to all periods presented in these financial statements, except for the changes related to IFRS 9 and IFRS 15 as explained in A3.1.

A4.1 Foreign currency transactions

Transactions in foreign currencies are translated into functional currency at the spot exchange rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated into the functional currency at the spot exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for the effective interest and payments during the period, and the amortised cost in the foreign currency translated at the spot exchange rate at the end of the period. The non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated into the functional currency at the spot exchange rate at the date the fair value was determined. Foreign currency differences arising on retranslation are recognised in the statement of comprehensive income, except for non-monetary financial assets, such as equities classified as available for sale (before 31 December 2017), which are included in other comprehensive income. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

A4 Significant accounting policies (continued)

A4.2 Revenue and expense recognition

A4.2.a Interest income and expense

Under both IFRS 9 and IAS 39, interest income and expense is recorded using the effective interest rate (EIR) method for all financial instruments measured at amortised cost and financial instruments designated at FVTPL. Interest income on interest bearing financial assets measured at FVOCI under IFRS 9, similarly to interest bearing financial assets classified as available-for-sale or held to maturity under IAS 39 are also recorded by using the EIR method. The EIR is the rate that exactly discounts estimated future cash 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. The calculation takes into account all contractual terms of the financial instrument and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the EIR, but not future credit losses.

The EIR (and therefore, the amortised cost of the asset) is calculated by taking into account any discount or premium on acquisition, fees and costs that are an integral part of the EIR. The Bank recognises interest income using a rate of return that represents the best estimate of a constant rate of return over the expected life of the loan. Hence, it recognises the effect of potentially different interest rates charged at various stages, and other characteristics of the product life cycle (including prepayments, penalty interest and charges).

Interest income which is doubtful of recovery is included in impairment allowance and excluded from income until it is received in cash.

When a financial asset becomes credit-impaired (as set out in Note A 4.3.g) and is, therefore, regarded as 'Stage 3', the Bank calculates interest income by applying the effective interest rate to the net amortised cost of the financial asset. If the financial assets cures (as outlined in Note 12.3.3.1) and is no longer credit-impaired, the Bank reverts to calculating interest income on a gross basis.

A4.2.b Fair value gains and losses

Fair value changes on derivatives held for risk management purposes and available for sale financial assets are presented in other comprehensive income.

Net income from financial assets at fair value through profit or loss, including all realised and unrealised fair value changes, interest, dividend and foreign exchange differences are presented in the income statement for the year.

A4.2.c Dividend income

Dividend income is recognised when the right to receive dividend is established.

A4.2.d Fees and commission

The Bank earns fee and commission income from a diverse range of services it provides to its customers. Fee income, which is not an integral part of the effective interest rate of a financial instrument, is accounted for in accordance with IFRS 15 'Revenue from Contracts with Customers'. Under the IFRS 15, fee income is measured by the Bank based on the consideration specified in a contract with a customer and excludes amounts collected on behalf of third parties. The Bank recognises revenue when it transfers control over a product or service to a customer.

Fees and commission income and expenses that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate.

Other fees and commission income – including account or loan servicing fees, advisory fee, investment management fees and sales commission– are recognised as the related services are performed. Loan syndication fees and placement fees are recognised when the loan has been arranged. Loan commitment fees for loans that are likely to be drawn down and other credit related fees are deferred (together with any incremental costs) and recognised as an adjustment to the EIR on the loan. When it is unlikely that a loan will be drawn down, the loan commitment fees are recognised over the commitment period on a straight line basis.

A4.2.e Provisions

A provision is recognised if, as a result of a past event, the Bank has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are equivalent to the amortised value of the future liabilities which is determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risk specific to the liability.

A4.2.f Offsetting of income and expense

Income and expenses are presented on a net basis only when permitted by the IFRS, or for gains and losses arising from a group of similar transactions such as in the Bank's trading activity.

A4 Significant accounting policies (continued)

A4.2 Revenue and expense recognition (continued)

A4.2.g Temporary significant influence

The Bank is exempt from applying the equity method when significant influence over an associate is intended to be temporary. The temporary significant influence infers that there is an evidence that an associate is acquired with the intention to reduce its stake that it no more has a significant influence on the investee company by soliciting investors to inject fresh capital to the investee company. The investment is classified as available for sale in the financial statements.

A4.3 Financial instruments

A4.3.a Date of recognition and initial measurement

The Bank initially recognises loans and advances, deposits, debt securities issued and subordinated liabilities on the date on which they originated. All other financial instruments (including regular-way purchases and sales of financial assets) are recognised on the trade date, which is the date on which the Bank becomes a party to the contractual provisions of the instrument.

A financial asset or financial liability is measured initially at fair value plus, for an item not at FVTPL, transaction costs that are directly attributable to its acquisition or issue. When the fair value of financial instruments at initial recognition differs from the transaction price, the Bank accounts for the Day 1 profit or loss, as described below.

A4.3.b Day 1 profit or loss

When the transaction price of the instrument differs from the fair value at origination and the fair value is based on a valuation technique using only inputs observable in market transactions, the Bank recognises the difference between the transaction price and fair value in net trading income. In those cases where fair value is based on models for which some of the inputs are not observable, the difference between the transaction price and the fair value is deferred and is only recognised in profit or loss when the inputs become observable, or when the instrument is derecognised.

A4.3.c Measurement categories of financial assets and liabilities

From 1 January 2018, the Bank classifies all of its financial assets based on the business model for managing the assets and the asset's contractual terms, measured at either:

- Amortised cost, as explained in note A4.3.c(i);
- FVOCI, as explained in notes A4.3.c (iv) and A4.3.c(v); or
- FVTPL, as explained in note A4.3.c(vii)

Before 1 January 2018, the Bank classified its financial assets as loans and receivables (amortised cost), FVPL, available-for-sale or held-to-maturity (amortised cost).

Financial liabilities, other than loan commitments and financial guarantees, are measured at amortised cost or at FVPL when they are held for trading and derivative instruments at the fair value designation.

The Bank classifies and measures its derivative and trading portfolio at FVTPL The Bank may designate financial instruments at FVTPL, if so doing eliminates or significantly reduces measurement or recognition inconsistencies.

(i) Due from banks and other money market placements, loans, advances and financing and, financial investments at amortised cost

Before 1 January 2018, due from banks and other money market placements and loans, advances and financing, included non–derivative financial assets with fixed or determinable payments that were not quoted in an active market, other than those:

- That the Bank intended to sell immediately or in the near term;
- That the Bank, upon initial recognition, designated as at FVTPL or as available-for-sale; or
- For which the Bank may not recover substantially all of its initial investment, other than because of credit deterioration, which were designated as available-for-sale.

A4 Significant accounting policies (continued)

A4.3 Financial instruments (continued)

A4.3.c Measurement categories of financial assets and liabilities (continued)

(i) Due from banks and other money market placements, loans, advances and financing and, financial investments at amortised cost (continued)

From 1 January 2018, the Bank only measures due from banks and other money market placements, loans, advances and financing and other financial investments at amortised cost if both of the following conditions are met:

- The financial asset is held within a business model with the objective to hold financial assets in order to collect contractual cash flows;
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest (SPPI) on the principal amount outstanding.

The details of these conditions are outlined below.

On initial recognition of an equity investment that is not held for trading, the Bank may irrevocably elect to present subsequent changes in fair value in OCI. This election is made on an investment-by-investment basis. All other financial assets are classified as measured at FVTPL.

In addition, on initial recognition, the Bank may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as at FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

- *Business model assessment*

The Bank makes an assessment of the objective of a business model in which an asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

- the stated policies and objectives for the portfolio and the operation of those policies in practice. In particular, whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realising cash flows through the sale of the assets;
- how the performance of the portfolio is evaluated and reported to the Bank's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed;
- how managers of the business are compensated – e.g. whether compensation is based on the fair value of the assets managed or the contractual cash flows collected; and
- the frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Bank's stated objective for managing the financial assets is achieved and how cash flows are realised**.**

The business model assessment is based on reasonably expected scenarios without taking 'worst case' or 'stress case' scenarios into account. If cash flows after initial recognition are realised in a way that is different from the Bank's original expectations, the Bank does not change the classification of the remaining financial assets held in that business model, but incorporates such information when assessing newly originated or newly purchased financial assets going forward.

Financial assets that are held for trading or managed and whose performance is evaluated on a fair value basis are measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

- *Assessment whether contractual cash flows are solely payments of principal and interest (The 'SPPI' test)*

For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition. 'Interest' is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest, the Bank considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Bank considers:

- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms;
- terms that limit the Bank's claim to cash flows from specified assets (e.g. non-recourse asset arrangements); and features that modify consideration of the time value of money – e.g. periodical reset of interest rates.

A4 Significant accounting policies (continued)

A4.3 Financial instruments (continued)

A4.3.c Measurement categories of financial assets and liabilities (continued)

(i) Due from banks and other money market placements, loans, advances and financing and, financial investments at amortised cost (continued)

The Bank holds a portfolio of long-term fixed rate loans for which the Bank has the option to propose to revise the interest rate at periodic reset dates. These reset rights are limited to the market rate at the time of revision. The borrowers have an option to either accept the revised rate or redeem the loan at par without penalty. The Bank has determined that the contractual cash flows of these loans are solely payments of principal and interest because the option varies the interest rate in a way that is consideration for the time value of money, credit risk, other basic lending risks and costs associated with the principal amount outstanding.

Contractual terms that introduce a more than de minimis exposure to risks or volatility in the contractual cash flows that are unrelated to a basic lending arrangement do not give rise to contractual cash flows that are solely payments of principal and interest on the amount outstanding. In such cases, the financial asset is required to be measured at FVPL.

(ii) Derivatives recorded at fair value through profit or loss

A derivative is a financial instrument or other contract with all three of the following characteristics:

- Its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable, provided that, in the case of a non-financial variable, it is not specific to a party to the contract (i.e., the 'underlying').
- It requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts expected to have a similar response to changes in market factors.
- It is settled at a future date.

The Bank enters into derivative transactions with various counterparties. These include interest rate swaps, futures, cross-currency swaps, forward foreign exchange contracts and options on interest rates, foreign currencies. Derivatives are recorded at fair value and carried as assets when their fair value is positive and as liabilities when their fair value is negative. The notional amount and fair value of such derivatives are disclosed separately in Note B24. Changes in the fair value of derivatives are included in net trading income unless hedge accounting is applied. Hedge documentation, effectiveness assessment, and discontinuation accounting disclosures are provided in Note A4.4.m.

Embedded derivatives:

Derivatives may be embedded in another contractual arrangement (a host contract). The Bank accounts for an embedded derivative separately from the host contract when:

- the host contract is not an asset in the scope of IFRS 9;
- the host contract is not itself carried at FVTPL;
- the terms of the embedded derivative would meet the definition of a derivative if they were contained in a separate contract; and
- the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract.

Separated embedded derivatives are measured at fair value, with all changes in fair value recognised in profit or loss unless they form part of a qualifying cash flow or net investment hedging relationship. Separated embedded derivatives are presented in the statement of financial position together with the host contract.

(iii) Financial assets or financial liabilities held for trading

The Bank classifies financial assets or financial liabilities as held for trading when they have been purchased or issued primarily for short-term profit making through trading activities or form part of a portfolio of financial instruments that are managed together, for which there is evidence of a recent pattern of short-term profit taking. Held-for-trading assets and liabilities are recorded and measured in the statement of financial position at fair value. Changes in fair value are recognised in other operating income. Interest and dividend income or expense is recorded in net trading income according to the terms of the contract, or when the right to payment has been established.

Included in this classification are debt securities, equities, short positions and customer loans that have been acquired principally for the purpose of selling or repurchasing in the near term.

A4 Significant accounting policies (continued)

A4.3 Financial instruments (continued)

A4.3.c Measurement categories of financial assets and liabilities (continued)

(iv) Debt instruments at FVOCI (Policy applicable from 1 January 2018)

The Bank applies the new category under IFRS 9 of debt instruments measured at FVOCI when both of the following conditions are met:

- The instrument is held within a business model, the objective of which is achieved by both collecting contractual cash flows and selling financial assets; and
- The contractual terms of the financial asset meet the SPPI test.

These instruments largely comprise assets that had previously been classified as financial investments available for sale under IAS 39.

For debt securities measured at FVOCI, gains and losses are recognised in OCI, except for the following, which are recognised in profit or loss in the same manner as for financial assets measured at amortised cost:

- interest revenue using the effective interest method;
- ECL and reversals; and
- foreign exchange gains and losses.

When debt security measured at FVOCI is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to profit or loss.

(v) Equity instruments at FVOCI (Policy applicable from 1 January 2018)

Upon initial recognition, the Bank occasionally elects to irrevocably classify some of its equity investments as equity instruments at FVOCI when they meet the definition of Equity under IAS 32 Financial Instruments: Presentation and are not held for trading. Such classification is determined on an instrument by instrument basis.

Gains and losses on these equity instruments are never recycled to profit. Dividends are recognised in profit or loss as other operating income when the right of the payment has been established, except when the Bank benefits from such proceeds as a recovery of part of the cost of the instrument, in which case, such gains are recorded in OCI. Equity instruments at FVOCI are not subject to an impairment assessment.

(vi) Debt issued and other borrowed funds

After initial measurement, debt issued and other borrowed funds are subsequently measured at amortised cost. Amortised cost is calculated by taking into account any discount or premium on issue funds, and costs that are an integral part of the EIR. A compound financial instrument which contains both a liability and an equity component is separated at the issue date.

(vii) Financial assets and financial liabilities at fair value through profit or loss

Financial assets and financial liabilities in this category are those that are not held for trading and have been either designated by management upon initial recognition or are mandatorily required to be measured at fair value under IFRS 9. Management only designates an instrument at FVTPL upon initial recognition when one of the following criteria is met. Such designation is determined on an instrument by instrument basis:

- The designation eliminates, or significantly reduces, the inconsistent treatment that would otherwise arise from measuring the assets or liabilities or recognising gains or losses on them on a different basis; or
- The liabilities (and assets until 1 January 2018 under IAS 39) are part of a group of financial liabilities (or financial assets, or both under IAS 39), which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management or investment strategy; or
- The liabilities (and assets until 1 January 2018 under IAS 39) containing one or more embedded derivatives, unless they do not significantly modify the cash flows that would otherwise be required by the contract, or it is clear with little or no analysis when a similar instrument is first considered that separation of the embedded derivative(s) is prohibited.

A4 Significant accounting policies (continued)

A4.3 Financial instruments (continued)

A4.3.c Measurement categories of financial assets and liabilities (continued)

(vii) Financial assets and financial liabilities at fair value through profit or loss (continued)

Financial assets and financial liabilities at FVTPL are recorded in the statement of financial position at fair value. Changes in fair value are recorded in profit and loss with the exception of movements in fair value of liabilities designated at FVTPL due to changes in the Bank's own credit risk. Such changes in fair value are recorded in the Own credit reserve through OCI and do not get recycled to the profit or loss. Interest earned or incurred on instruments designated at FVTPL is accrued in interest income or interest expense, respectively, using EIR, taking into account any discount/premium and qualifying transaction costs being an integral part of instrument. Interest earned on assets mandatorily required to be measured at FVTPL is recorded using contractual interest rate. Dividend income from equity instruments measured at FVTPL is recorded in profit or loss as other operating income when the right to the payment has been established.

(viii) Financial guarantees, letters of credit and undrawn loan commitments

The Bank issues financial guarantees, letters of credit and loan commitments.

Financial guarantees are initially recognised in the financial statements (within Provisions) at fair value, being the premium received. Subsequent to initial recognition, the Bank's liability under each guarantee is measured at the higher of the amount initially recognised less cumulative amortisation recognised in the income statement, and – under IAS 39 – the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee, or – under IFRS 9 – an ECL provision as set out in Note A4.3.f.

The premium received is recognised in the income statement in Net fees and commission income on a straight line basis over the life of the guarantee.

Undrawn loan commitments and letters of credits are commitments under which, over the duration of the commitment, the Bank is required to provide a loan with pre-specified terms to the customer. Similar to financial guarantee contracts, under IAS 39, a provision was made if they were an onerous contract but, from 1 January 2018, these contracts are in the scope of the ECL requirements.

The nominal contractual value of financial guarantees, letters of credit and undrawn loan commitments, where the loan agreed to be provided is on market terms, are not recorded on in the statement of financial position.

(ix) Financial liabilities

IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities. However, although under IAS 39 all fair value changes of liabilities designated under the fair value option were recognised in profit or loss, under IFRS 9 fair value changes are generally presented as follows:

- the amount of change in the fair value that is attributable to changes in the credit risk of the liability is presented in OCI; and
- the remaining amount of change in the fair value is presented in profit or loss.

The amount presented separately in OCI related to changes in own credit risk of a designated financial liability at FVTPL are not recycled to profit or loss, even when the liability is derecognised and the amounts are paid. Instead, own credit gains and losses should be reclassified to retained earnings within equity upon derecognition of the relevant liability.

(x) Available for sale financial investments (Policy applicable before 1 January 2018)

Available for sale financial assets include equity and debt securities. Equity investments classified as available for sale are those which are neither classified as held for trading nor designated at fair value through profit or loss. Debt securities in this category are intended to be held for an indefinite period of time and may be sold in response to needs for liquidity or in response to changes in the market conditions.

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

After initial measurement, available for sale financial investments are subsequently measured at fair value.

Unrealised gains and losses are recognised directly in equity (other comprehensive income) in the change in fair value of available for sale financial assets. When the investment is disposed of, the cumulative gain or loss previously recognised in equity is recognised in the profit or loss in other operating income. Interest earned whilst holding available for sale financial investments is reported as interest income using the EIR. Dividends earned whilst holding available for sale financial investments are recognised in the profit or loss as other operating income when the right of the payment has been established. The losses arising from impairment of such investments are recognised in the profit or loss in impairment for available for sale financial assets and removed from the change in fair value of investments available for sale.

A4 Significant accounting policies (continued)

A4.3 Financial instruments (continued)

A4.3.c Measurement categories of financial assets and liabilities (continued)

(xi) Held to maturity financial investments (Policy applicable before 1 January 2018)

Held to maturity financial assets are non-derivative assets with fixed or determinable payments and fixed maturity that the Bank has the positive intent and ability to hold to maturity and which are not designated at fair value through profit or loss or available for sale.

These are initially recognised at fair value including direct and incremental transaction costs and measured subsequently at amortised cost, using the effective interest method.

Interest on held to maturity investments is included in the statement of comprehensive income and reported as 'interest income'. In the case of impairment, the impairment loss is been reported as a deduction from the carrying value of the investment and recognised in the statement of comprehensive income as 'impairment for investments'.

A4.3.d Derecognition

(i) Financial assets

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

- The rights to receive cash flows from the asset have expired; or
- The Bank has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass–through' arrangement; and either:

  - The Bank has transferred substantially all the risks and rewards of the asset; or
  - The Bank has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset

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

Fore derecognition due to substantial modification, refer note A4.3p.

(ii) Financial liabilities

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

A4.3.e Offsetting of financial assets and financial liabilities

Financial assets and financial liabilities are only offset and the net amount reported in the statement of financial position when there is a legally enforceable right to set off the recognised amounts and the Bank intends to either settle on a net basis or to realise the asset and settle the liability simultaneously. Income and expenses are presented on a net basis only when permitted by the accounting standards or for gains and losses arising from a group of similar transactions.

A4 Significant accounting policies (continued)

A4.3 Financial instruments (continued)

A4.3.f Impairment of financial assets (Policy applicable from 1 January 2018)

The Bank recognises loss allowances for ECL on the following financial instruments that are not measured at FVTPL:

- financial assets that are debt instruments;
- financial guarantee contracts issued; and
- loan commitments issued.

No impairment loss is recognised on equity investments. The Bank measures loss allowances at an amount equal to lifetime ECL, except for other financial instruments on which credit risk has not increased significantly since their initial recognition which they are measured as 12-month ECL.

12-month ECL are the portion of ECL that result from default events on a financial instrument that are possible within the 12 months after the reporting date.

(i) Measurement of ECL

ECL are a probability-weighted estimate of credit losses. They are measured as follows:

- financial assets that are not credit-impaired at the reporting date: as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Bank expects to receive);
- financial assets that are credit-impaired at the reporting date: as the difference between the gross carrying amount and the present value of estimated future cash flows;
- undrawn loan commitments: as the present value of the difference between the contractual cash flows that are due to the Bank if the commitment is drawn down and the cash flows that the Bank expects to receive; and
- financial guarantee contracts: the expected payments to reimburse the holder less any amounts that the Bank expects to recover.

(ii) Overview of the ECL principles

The adoption of IFRS 9 has fundamentally changed the Bank's loan loss impairment method by replacing IAS 39's incurred loss approach with a forward-looking ECL approach. From 1 January 2018, the Bank has been recording the allowance for expected credit losses for all loans and other debt financial assets not held at FVTPL, together with loan commitments and financial guarantee contracts, in this section all referred to as 'financial instruments'. Equity instruments are not subject to impairment under IFRS 9.

The ECL allowance is based on the credit losses expected to arise over the life of the asset (the lifetime expected credit loss or LTECL), unless there has been no significant increase in credit risk since origination, in which case, the allowance is based on the 12 months' expected credit loss (12mECL).

The 12mECL is the portion of LTECLs that represent the ECLs that result from default events on a financial instrument that are possible within the 12 months after the reporting date.

Both LTECLs and 12mECLs are calculated on either an individual basis or a collective basis, depending on the nature of the underlying portfolio of financial instruments.

The Bank has established a policy to perform an assessment, at the end of each reporting period, of whether a financial instrument's credit risk has increased significantly since initial recognition, by considering the change in the risk of default occurring over the remaining life of the financial instrument.

Based on the above process, the Bank groups its loans into Stage 1, Stage 2, Stage 3 and POCI, as described below:

Stage 1
When financing are first recognised, the Bank recognises an allowance based on 12 month ECLs. Stage 1 financing exposure also include facilities where the credit risk has improved and the financing exposure has been reclassified from Stage 2.

Stage 2
When a financing exposure has shown a significant increase in credit risk since origination, the Bank records an allowance for the LTECLs. Stage 2 financing exposure also include facilities, where the credit risk has improved and the financing exposure has been reclassified from Stage 3.

A4 Significant accounting policies (continued)

A4.3 Financial instruments (continued)

A4.3.f Impairment of financial assets (Policy applicable from 1 January 2018) (continued)

Stage 3
Financing exposure considered credit-impaired. The Bank records an allowance for the LTECLs.

At initial recognition of a financial asset, the Bank recognises a loss allowance equal to 12-month expected credit losses. After initial recognition, the three stages under the proposals would be applied as follows:

Stage 1
Credit risk has not increased significantly since initial recognition – recognise 12-month expected credit losses

Stage 2
Credit risk has increased significantly since initial recognition – recognise lifetime expected losses (this is recognising a provision earlier than under IAS 39 Financial assets: Recognition and Measurement) with revenue being calculated based on the gross amount of the asset

Stage 3
There is objective evidence of impairment as at the reporting date to recognise lifetime expected losses, with revenue being based on the net amount of the asset (that is, based on the impaired amount of the asset).

(iii) The calculation of ECLs

The Bank calculates ECLs based on a three probability-weighted scenarios to measure the expected cash shortfalls, discounted at an approximation to the EIR. A cash shortfall is the difference between the cash flows that are due to an entity in accordance with the contract and the cash flows that the entity expects to receive.

The mechanics of the ECL calculations are outlined below and the key elements are, as follows:

- PD - The Probability of Default is an estimate of the likelihood of default over a given time horizon. A default may only happen at a certain time over the assessed period, if the facility has not been previously derecognised and is still in the portfolio.
- EAD - The Exposure at Default is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date, including repayments of principal and interest, whether scheduled by contract or otherwise, expected drawdowns on committed facilities, and accrued interest from missed payments.
- LGD - The Loss Given Default is an estimate of the loss arising in the case where a default occurs at a given time. It is based on the difference between the contractual cash flows due and those that the Bank would expect to receive, including from the realisation of any collateral. It is usually expressed as a percentage of the EAD.

(iv) Presentation of allowanace for ECL in the statement of financial position

Loss allowances for ECL are presented in the statement of financial position as follows:

- financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets;
- loan commitments and financial guarantee contracts: generally, as a provision;
- where a financial instrument includes both a drawn and an undrawn component, and the Bank cannot identify the ECL on the loan commitment component separately from those on the drawn component: the Bank presents a combined loss allowance for both components. The combined amount is presented as a deduction from the gross carrying amount of the drawn component. Any excess of the loss allowance over the gross amount of the drawn component is presented as a provision; and
- debt instruments measured at FVOCI: no loss allowance is recognised in the statement of financial position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognised in the fair value reserve.

(v) Debt instruments measured at fair value through OCI

The ECLs for debt instruments measured at FVOCI do not reduce the carrying amount of these financial assets in the statement of financial position, which remains at fair value. Instead, an amount equal to the allowance that would arise if the assets were measured at amortised cost is recognised in OCI as an accumulated impairment amount, with a corresponding charge to profit or loss. The accumulated loss recognised in OCI is recycled to the profit and loss upon derecognition of the assets.

A4 Significant accounting policies (continued)

A4.3 Financial instruments (continued)

A4.3.f Impairment of financial assets (Policy applicable from 1 January 2018) (continued)

(vi) Purchased or originated credit impaired financial assets (POCI)

For POCI financial assets, the Bank only recognises the cumulative changes in LTECL since initial recognition in the loss allowance.

(vii) Credit cards and other revolving facilities

The Bank's product offering includes a variety of corporate and retail overdraft and credit cards facilities, in which the Bank has the right to cancel and/or reduce the facilities with one day's notice. The Bank does not limit its exposure to credit losses to the contractual notice period, but, instead calculates ECL over a period that reflects the Bank's expectations of the customer behaviour, its likelihood of default and the Bank's future risk mitigation procedures, which could include reducing or cancelling the facilities.

The ongoing assessment of whether a significant increase in credit risk has occurred for revolving facilities is similar to other lending products. This is based on shifts in the customer's internal credit grade, but greater emphasis is also given to qualitative factors such as changes in usage.

The interest rate used to discount the ECLs for credit cards is based on the average effective interest rate that is expected to be charged over the expected period of exposure to the facilities. This estimation takes into account that many facilities are repaid in full each month and are consequently charged no interest.

(viii) Forward looking information

In its ECL models, the Bank relies on a broad range of forward looking information as economic inputs, such as:

- Gross domestic product
- Savings and investment
- Inflation
- Trade statistics
- Demographics
- Revenue and expenditure
- Public debt
- Real estate
- Composite indicators
- Oil prices and production

The inputs and models used for calculating ECLs may not always capture all characteristics of the market at the date of the financial statements. To reflect this, qualitative adjustments or overlays are occasionally made as temporary adjustments when such differences are significantly material.

(ix) Collateral valuation

To mitigate its credit risks on financial assets, the Bank seeks to use collateral, where possible. The collateral comes in various forms, such as cash, securities, letters of credit/guarantees, real estate, receivables, inventories, other non-financial assets and credit enhancements such as netting agreements. The Bank's accounting policy for collateral assigned to it through its lending arrangements under IFRS 9 is the same as it was under IAS 39. Collateral, unless repossessed, is not recorded on the Bank's statement of financial position. However, the fair value of collateral affects the calculation of ECLs. It is generally assessed, at a minimum, at inception and re-assessed periodically based on the type of asset, for example, cash or securities relating to margining requirements, is valued daily.

To the extent possible, the Bank uses active market data for valuing financial assets held as collateral. Non-financial collateral, such as real estate, is valued by certified third party valuers.

(x) Write-offs

The Bank's accounting policy under IFRS 9 remains the same as it was under IAS 39. Loans and debt securities are written off (either partially or in full) when there is no realistic prospect of recovery. This is generally the case when the Bank determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. However, financial assets that are written off could still be subject to enforcement activities in order to comply with the Bank's procedures for recovery of amounts due.

A4 Significant accounting policies (continued)

A4.3 Financial instruments (continued)

A4.3.f Impairment of financial assets (Policy applicable from 1 January 2018) (continued)

(xi) Assets carried at amortised cost (Policy applicable before 1 January 2018)

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 or held to maturity investments carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the statement of comprehensive income. If a loan or held to maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract.

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.

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 group and historical loss experience for assets with credit risk characteristics similar to those in the group.

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 uncollectible, it is written off against the related allowance 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.

If in a subsequent period, the amount of impairment loss decreases and decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the statement of comprehensive income. Also refer to note B3 for loans, advances and financing.

(xii) Assets classified as available for sale (Policy applicable before 1 January 2018)

The Bank assesses at the end of each reporting period whether there is objective evidence that a financial asset or a group of financial assets is impaired. For debt securities, the Bank uses the criteria referred to at (i) above. 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 evidence that 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 profit or loss. Impairment losses on equity instruments recognised in the profit or loss are not reversed through statement of profit or loss.

A4.3.g Restructured financial assets

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognized and ECL are measured as follows.

- If the expected restructuring will not result in derecognition of the existing asset, then the expected cash flows arising from the modified financial asset are included in calculating the cash shortfalls from the existing asset.
- If the expected restructuring will result in derecognition of the existing asset, then the expected amortised fair value of the new asset is treated as the final cash flow from the existing financial asset at the time of its derecognition. This amount is included in calculating the cash shortfalls from the existing financial asset that are discounted from the expected date of derecognition to the reporting date using the original effective interest rate of the existing financial asset.

A4 Significant accounting policies (continued)

A4.3 Financial instruments (continued)

A4.3.h Credit-impaired financial assets

At each reporting date, the Bank assesses whether financial assets carried at amortised cost and debt financial assets carried at FVOCI are credit-impaired. A financial asset is 'credit-impaired' when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred.

Evidence that a financial asset is credit-impaired includes the following observable data:

- significant financial difficulty of the borrower or issuer;
- a breach of contract such as a default or past due event;
- the restructuring of a loan or advance by the Bank on terms that the Bank would not consider otherwise;
- it is becoming probable that the borrower will enter bankruptcy or other financial reorganisation; or
- the disappearance of an active market for a security because of financial difficulties.

A loan that has been renegotiated due to a deterioration in the borrower's condition is usually considered to be credit-impaired unless there is evidence that the risk of not receiving contractual cash flows has reduced significantly and there are no other indicators of impairment. In addition, a retail loan that is overdue for 90 days or more is considered impaired.

In making an assessment of whether an investment in sovereign debt is credit-impaired, the Bank considers the following factors.

- The market's assessment of creditworthiness as reflected in the bond yields.
- The rating agencies' assessments of creditworthiness.
- The country's ability to access the capital markets for new debt issuance.
- The probability of debt being restructured, resulting in holders suffering losses through voluntary or mandatory debt forgiveness.
- The international support mechanisms in place to provide the necessary support as 'lender of last resort' to that country, as well as the intention, reflected in public statements, of governments and agencies to use those mechanisms. This includes an assessment of the depth of those mechanisms and, irrespective of the political intent, whether there is the capacity to fulfil the required criteria.

A4.3.i Amortised cost measurement

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest rate of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

A4.3.j Fair value measurement

A number of the Bank's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on a number of accounting policies and methods. Where applicable, information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability, or
- In the absence of a principal market, in the most advantageous market for the asset or liability

The principal or the most advantageous market must be accessible to the Bank. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Bank uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

A4 Significant accounting policies (continued)

A4.3 Financial instruments (continued)

A4.3.j Fair value measurement (continued)

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1 — Quoted (unadjusted) market prices in active markets for identical assets or liabilities
- Level 2 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable
- Level 3 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Bank determines whether transfers have occurred between Levels in the hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

At each reporting date, the Bank analyses the movements in the values of assets and liabilities which are required to be re-measured or re-assessed as per the Bank's accounting policies. For this analysis, the Bank verifies the major inputs applied in the latest valuation by agreeing the information in the Valuation computation to contracts and other relevant documents.

The Bank also compares the changes in the fair value of each asset and liability with relevant external sources to determine whether the change is reasonable.

For the purpose of fair value disclosures, the Bank has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy as explained above.

A4.3.k Cash and cash equivalents

Cash and cash equivalents consist of cash in hand, unrestricted balances held with central banks and highly liquid financial assets with original maturities of up to three months, which are subject to insignificant risk of changes in their fair value, and are used by the Bank in management of its short term commitments. Cash and cash equivalents are carried at amortised cost in the statement of financial position.

A4.3.l Repurchase and resale agreements

Securities sold with a commitment to repurchase (repos) at a specified future date are recognised in the statement of financial position and are measured in accordance with accounting policies for trading securities or investment securities. The counterparty liability for amounts received under these agreements is included in 'due to banks and other money market borrowings'. The difference between sale and repurchase price is treated as interest expense and accrued over the life of the repo agreement.

Securities purchased with a corresponding commitment to resell at a specified future date (reverse repos) are not recognised in the statement of financial position and the amounts paid under these agreements are included in 'due from banks and other money market placements'. The difference between purchase and resale price is treated as interest income and accrued over the life of the reverse repo agreement.

A4.3.m Acceptances

Acceptances are disclosed on the statement of financial position under other assets with corresponding liability disclosed under other liabilities. Therefore, there is no off-balance sheet commitment for acceptances.

A4 Significant accounting policies (continued)

A4.3 Financial instruments (continued)

A4.3.n Derivatives held for risk management purposes

Derivatives held for risk management purposes include all derivative assets and liabilities that are not classified as trading assets or trading liabilities. Derivatives held for risk management purposes are measured at fair value in the statement of financial position. The treatment of changes in their fair value depends on their classification into the following categories:

(i) Fair value hedge

When a derivative is designated as a hedge of the change in fair value of a recognised asset or liability or a firm commitment, changes in the fair value of the derivative are recognised immediately in statement of comprehensive income together with changes in the fair value of the hedged item that are attributable to the hedged risk.

If the derivative expires or is sold, terminated, or exercised, no longer meets the criteria for fair value hedge accounting, or the designation is revoked, hedge accounting is discontinued. Any adjustment up to that point, to a hedged item for which the effective interest method is used, is amortised to profit or loss as part of the recalculated effective interest rate of the item over its remaining life.

(ii) Cash flow hedge

When a derivative is designated as the hedging instrument in a hedge of the variability in cash flows attributable to a particular risk associated with a recognised asset or a liability or a highly probable forecast transaction that could affect profit or loss, the effective portion of changes in the fair value of the derivative is recognised in other comprehensive income in hedging reserve. The amount recognised in other comprehensive income is reclassified to profit or loss as a reclassification adjustment in the same period as the hedged cash flows affect profit or loss, and in the same line item in the statement of comprehensive income. Any ineffective portion of changes in the fair value of the derivative is recognised immediately in profit or loss.

If the hedging derivative expires or is sold, terminated, or exercised, or the hedge no longer meets the criteria for cash flow hedge accounting, or the hedge designation is revoked, then the hedge accounting is discontinued prospectively. In a discontinued hedge of a forecast transaction the cumulative amount recognised in other comprehensive income from the period when the hedge was effective is reclassified from the equity to statement of comprehensive income as a reclassification adjustment when the forecast transaction occurs and affects profit or loss. If the forecast transaction is no longer expected to occur, then the balance in other comprehensive income is reclassified immediately to profit or loss as a reclassification adjustment.

(iii) Other non-trading derivative

When a derivative is not held for trading, and is not designated in a qualifying hedge relationship, all changes in its fair value are recognised immediately in statement of comprehensive income.

A4.3.o Reclassifications

From 1 January 2018, the Bank does not reclassify its financial assets subsequent to their initial recognition, except in the period after the Bank changes its business model for managing financial assets. Financial liabilities are never reclassified. The Bank did not reclassify any of its financial assets or liabilities in 2017.

A4.3.p Modifications of financial assets and liabilities

Financial assets
If the terms of a financial asset are modified, the bank evaluates whether the cash flows of the modified asset are substantially different. If the cash flows are substantially different, the original financial asset is derecognised and a new financial asset is recognised at fair value. If the cash flows are not substantially different, then the modification does not result in derecognition of the financial asset. In this case, the bank recalculates the gross carrying amount of the financial asset and recognises the amount arising from adjusting the gross carrying amount as a modification gain or loss in the statement of income. If such a modification is carried out because of financial difficulties of the borrower, then the gain or loss is presented together with impairment losses. In other cases, it is presented as interest income.

If the terms of a financial asset were modified because of financial difficulties of the borrower and the asset was not derecognised, then impairment of the asset was measured using the pre-modification interest rate.

Financial liabilities
The bank derecognises a financial liability when its terms are modified and the cash flows of the modified liability are substantially different. In this case, a new financial liability based on the modified terms is recognised at either amortised cost or fair value. The difference between the carrying amount of the financial liability derecognised and the new financial liability with modified terms is recognised in the statement of income.

A4 Significant accounting policies (continued)

A4.4 Property, equipment and fixtures

Items of property, equipment and fixtures are measured at historical cost less accumulated depreciation and impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the asset and preparing the asset for its intended use. Depreciation is provided on a straight-line basis over the estimated useful lives of property, equipment and fixtures, except freehold land. The estimated useful lives for the current year are as follows:

Asset	Years
Motor vehicles	5
Furniture and fixtures	6-7
Office equipment	6-7
Production software	10

Land and capital work in progress are not depreciated, but tested for impairment. The assets' residual values, useful lives and depreciation methods are reviewed and adjusted if appropriate at each reporting date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised within 'other operating income' in the statement of comprehensive income.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance are charged to the profit or loss during the financial period in which they are incurred.

A4.5 Investment properties

Investment properties comprise plots of land received by the Bank as grant from the Government of Sultanate of Oman during the year 2008. These are currently held for an undetermined business use and not occupied by the Bank. These are carried at the average valuation of the two professional valuators carried out during 2008. Subsequent to initial measurement these properties are carried at cost less accumulated impairments, if any.

A4.6 Deposits, debt securities issued and subordinated liabilities

All money market and customer deposits are initially measured at fair value plus transaction cost and subsequently carried at amortised cost. Deposits, debt securities issued and subordinated liabilities are measured at their amortised cost using the effective interest method. The Bank classifies capital instruments as financial liabilities or equity instruments in accordance with the substance of the contractual terms of the instrument.

A4.7 Taxation

Taxation is provided in accordance with Omani fiscal regulations. Income tax comprises current and deferred tax. Income tax expense is recognised in the statement of comprehensive income except to the extent that it relates to items recognised directly in equity or other comprehensive income.

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

Deferred tax assets/liabilities are calculated using the liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to the temporary difference when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

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

A4 Significant accounting policies (continued)

A4.8 Fiduciary assets

Assets held in trust or in a fiduciary capacity are not treated as assets of the Bank and accordingly are not included in these financial statements.

A4.9 Leases

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

A4.10 Financial guarantees

Financial guarantees are contracts that require the issuer to make specified payments to reimburse the beneficiary for a loss incurred because the debtor fails to make payments when due, in accordance with the terms of the debt. Such guarantees are given to banks, financial institutions or other entities on behalf of the customers.

Financial guarantees are initially recognised in the financial statements at fair value on the date the guarantee was issued. Subsequent to initial recognition, the Bank's liabilities under such guarantees are measured at the higher of initial measurement, less amortisation calculated to recognise in the statement of comprehensive income the fee income earned on the straight line basis over the life of the guarantee and the best estimate of the expenditure required to settle any financial obligation arising at the reporting date. These estimates are determined based on experience of similar transactions and history of past losses, supplemented by the judgment of management. Any increase in the liability relating to guarantees is taken to the statement of comprehensive income.

A4.11 Employee benefits

A4.11.a Terminal benefits

End of service benefits are accrued in accordance with the terms of employment of the Bank's employees at the reporting date, having regard to the requirements of the Oman Labour Law 2003, as amended.

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

A4.11.b Short term benefits

Short term benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

A provision is recognised for the amount expected to be paid if the Bank has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

A4.12 Earnings per share

The Bank presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Bank by the weighted average number of ordinary shares outstanding during the year. Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares, which comprise convertible notes or similar instruments.

A4.13 Dividend on ordinary shares

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

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

A4.14 Segment reporting

An operating segment is the component of the Bank that engages in business activities from which it may earn revenues and incur expenses, including revenue and expenses that relate to transactions with any of the Bank's other components, whose operating results are reviewed regularly by the Bank's CEO (being the chief operating decision maker) to make decisions about resources allocated to each segment and assess its performance, and for which discrete financial information is available.

A4 Significant accounting policies (continued)

A4.15 Directors' remuneration and sitting fees

The Directors' remuneration is governed as set out in the Commercial Companies Law, regulations issued by the Capital Market Authority and the Articles of Association of the Company.

The Annual General Meeting determines and approves the remuneration and the sitting fees for the Board of Directors and its sub-committees provided such fees, in accordance with Article 106 of the Commercial Companies Law of Oman of 1974 as amended, shall not exceed 5% of the annual net profit after deduction of the legal reserve and the optional reserve and the distribution of dividends to the shareholders provided that such fees does not exceed RO 200,000. The sitting fee for each Director does not exceed RO 10,000 in one year.

A4.16 Perpetual Tier I Capital Securities

The Bank classifies Perpetual Tier I Capital Securities as financial liabilities or equity instruments in accordance with the substance of the contractual terms of the Tier I Capital Securities. The Bank's Perpetual Tier I Capital Securities are not redeemable by holders and bear an entitlement to distribution that is non-cumulative and at the discretion of the Board of Directors. Accordingly, they are presented as component within equity.

A5 Critical accounting estimates and judgements

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and reported amounts of assets, liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. The resulting accounting estimates will, by definition, seldom equal the related actual results.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods. The Bank's significant accounting estimates are on:

A5.1 Financial Instruments (applicable from 1 January 2018)

Judgements made in applying accounting policies that have most significant effects on the amounts recognized in the financial statements of the year ended 31 December 2018 pertain to the changes introduced as a result of adoption of IFRS 9: Financial instruments which impact:

- Classification of financial assets: assessment of business model within which the assets are held and assessment of whether the contractual terms of the financial assets are solely payment of principal and interest of the principal amount outstanding.

- Calculation of expected credit loss (ECL): changes to the assumptions and estimate on uncertainties that have a significant impact on ECL for the year ended 31 December 2018 pertain to the changes introduced as a result of adoption of IFRS 9: Financial instruments. The impact is mainly driven by inputs, assumptions and techniques used for ECL calculation under IFRS 9 methodology.

Inputs, assumptions and techniques used for ECL calculation – IFRS 9 Methodology

The measurement of impairment losses both under IFRS 9 and IAS 39 across all categories of financial assets requires judgement, in particular, the estimation of the amount and timing of future cash flows and collateral values when determining impairment losses and the assessment of a significant increase in credit risk. These estimates are driven by a number of factors, changes in which can result in different levels of allowances. The Bank's ECL calculations are outputs of complex models with a number of underlying assumptions regarding the choice of variable inputs and their interdependencies. Elements of the ECL models that are considered accounting judgements and estimates include:

- The Bank's internal credit grading model, which assigns PDs to the individual grades;
- The Bank's criteria for assessing if there has been a significant increase in credit risk and so allowances for financial assets should be measured on a LTECL basis and the qualitative assessment;
- The segmentation of financial assets when their ECL is assessed on a collective basis;
- Development of ECL models, including the various formulas and the choice of inputs;
- Determination of associations between macroeconomic scenarios and economic inputs, such as unemployment levels and collateral values, and the effect on PDs, EADs and LGDs; and
- Selection of forward-looking macroeconomic scenarios and their probability weightings, to derive the economic inputs into the ECL models.

A5 Critical accounting estimates and judgements (continued)

A5.2 Fair value of derivatives and other financial instruments

The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined by using valuation techniques. The Bank uses its judgement to select a variety of methods and makes assumptions that are mainly based on market conditions existing at the end of each reporting period. The Bank uses expected cash flow analysis for certain available for sale financial assets that are not traded in active markets.

A5.3 Taxation

Uncertainties exist with respect to the interpretation of tax regulations and the amount and timing of future taxable income. Given the wide range of business relationships and nature of existing contractual agreements, differences arising between the actual results and the assumptions made, or future changes to such assumptions, could necessitate future adjustments to tax income and expense already recorded. The Bank establishes provisions, based on reasonable estimates, for possible consequences of finalisation of tax assessments of the Bank. The amount of such provisions is based on various factors, such as experience of previous tax assessments and differing interpretations of tax regulations by the taxable entity and the responsible tax authority.

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

A5.4 Fair value estimation of unquoted securities

In cases where the underlying assets are fair valued such as private equity funds, management uses net assets value. Management believes that net assets values of these investments are representative of their fair values as the majority of the underlying assets are fair valued and the reported net assets of those entities takes into account the updated fair values changes.

A5.5 Fee and commission income

The recognition of fee and commission income depends on the purpose for which fees are assessed and the basis of accounting for any associated financial instrument. Management applies certain assumptions and judgements to determine the fees that are an integral part of the effective interest rate of a financial instrument, fees that are earned as services are provided, and fees that are earned on the execution of a significant act.

A6 Transition disclosures

Impact of adopting IFRS 9
The following pages set out the impact of adopting IFRS 9 on the statement of financial position, and retained earnings including the effect of replacing IAS 39's incurred credit loss model with IFRS 9's ECLs.

A6.1 The impact of transition to IFRS 9 on reserves and retained earnings is as follows:

	Retained earnings RO'000	Special reserve RO'000	Fair value reserve RO'000
Closing balance under IAS 39 (31 December 2017)	**72,651**	**3,103**	**(656)**
<u>Impact on reclassification and remeasurement (i):</u>			
Reclassification of debt securities from available for sale to amortised cost	-	-	**314**
Reclassification of investment securities from available for sale to FVTPL	**(292)**	-	**292**
Reclassification of equity securities from available for sale to FVOCI	**2,547**	-	**(2,547)**
Deferred tax in relation to the above	-	-	**(94)**
<u>Impact on recognition of Expected Credit Losses(ii):</u>			
Due from banks, Central Bank and other financial assets	**(281)**	-	-
Loan and advances at amortised cost, including loan commitments and financial guarantees	**(21,441)**	-	-
Utilisation of special reserve towards loan and advances at amortised cost, including loan commitments and financial guarantees	**3,103**	**(3,103)**	-
Debt securities at amortised cost	**(332)**	-	-
Debt securities at FVOCI	**(17)**	-	**17**
Adjusted opening balance under IFRS 9 on date of initial application of 1 January 2018	**55,938**	-	**(2,674)**

	Retained earnings USD'000	Special reserve USD'000	Fair value reserve USD'000
Closing balance under IAS 39 (31 December 2017)	**188,704**	**8,060**	**(1,704)**
<u>Impact on reclassification and remeasurement (i):</u>			
Reclassification of debt securities from available for sale to amortised cost	-	-	**815**
Reclassification of investment securities from available for sale to FVTPL	**(758)**	-	**758**
Reclassification of equity securities from available for sale to FVOCI	**6,615**	-	**(6,615)**
Deferred tax in relation to the above	-	-	**(244)**
<u>Impact on recognition of Expected Credit Losses(ii):</u>			
Due from banks, Central Bank and other financial assets	**(730)**	-	-
Loan and advances at amortised cost, including loan commitments and financial guarantees	**(55,691)**	-	-
Utilisation of special reserve towards loan and advances at amortised cost, including loan commitments and financial guarantees	**8,060**	**(8,060)**	-
Debt securities at amortised cost	**(862)**	-	-
Debt securities at FVOCI	**(44)**	-	**44**
Adjusted opening balance under IFRS 9 on date of initial application of 1 January 2018	**145,294**	-	**(6,946)**

A6 Transition disclosures (continued)

(i) Classification and measurement of financial instruments

The Bank performed a detailed analysis of its business models for managing financial assets as well as analysing their cash flow characteristics. The below table reconciles the original measurement categories and carrying amounts of financial assets in accordance with IAS 39 and the new measurement categories under IFRS 9 as at 31 December 2017.

					Impact of IFRS 9	
	Original classification under IAS 39	**New classification under IFRS 9**	**Original carrying amount**	**Re-measurement**	**Reclassification**	**New carrying amount**
			RO'000	**RO'000**	**RO'000**	**RO'000**
Financial assets						
Cash and balances with central bank	AC	AC	**182,324**	**-**	**-**	**182,324**
Due from banks and other money market placements	AC	AC	**104,203**	**(281)**	**-**	**103,921**
Loans, advances and financing, net	AC	AC	**2,098,748**	**(18,948)**	**-**	**2,079,800**
Investment securities – debt	AFS	AC	**4,344**	**-**	**(4,344)**	**-**
Investment securities – debt	AFS	FVOCI	**185,050**	**-**	**-**	**185,050**
Investment securities – debt	AFS	FVTPL	**-**	**-**	**6,297**	**6,297**
Investment securities – debt	HTM	AC	**89,686**	**(332)**	**4,658**	**94,012**
Investment securities – debt	HFT	FVTPL	**105,372**	**-**	**-**	**105,372**
Investment securities – debt	HFT	FVOCI	**5,328**	**-**	**-**	**5,328**
Investment securities – equity	AFS	FVOCI	**23,961**	**-**	**(6,297)**	**17,664**
Investment securities – equity	AFS	FVTPL	**-**	**-**	**-**	**-**
Other assets	AC	AC	**22,049**	**(94)**	**-**	**21,955**
Accrued interest receivable	AC	AC	**-**	**-**	**-**	**-**
Derivatives with positive fair value	FVTPL	FVTPL	**1,744**	**-**	**-**	**1,744**
Other balance sheet items						
Commitments, contingent liabilities and financial guarantees etc.	NA	NA	**-**	**(2,493)**	**-**	**(2,493)***
Net Impact			**2,822,809**	**(22,148)**	**314**	**2,800,975**

*ECL provision for commitments, contingent liabilities and financial guarantees etc. has been recognised under 'other liabilities'.

L&R ff– Loans and receivables; AFS – Available for sale; HFT – Held for trading; AC – Amortised cost; FVTPL – Fair value through profit and loss; FVOCI – Fair value through other comprehensive income

Financial liabilities

There were no changes to the classification and measurement of financial liabilities.

A6 Transition disclosures (continued)
(ii) Expected credit loss/ impairment allowances

The following table reconciles the closing impairment allowance for financial assets in accordance with IAS 39 as at 31 December 2017 to the opening ECL allowance determined in accordance with IFRS 9 as at 1 January 2018:

	31 December 2017 RO'000	Re-measurement RO'000	1 January 2018 RO'000
Due from Banks, Central Banks and Other Financial Assets	1,039	281	1,320
Loan and advances at amortised cost (B3)	42,946	18,948	61,894
Loan commitments and financial guarantees (B10)	-	2,493	2,493
Debt securities at amortised cost	-	332	332
	43,985	22,054	66,039

	31 December 2017 USD'000	Re-measurement USD'000	1 January 2018 USD'000
Due from Banks, Central Banks and Other Financial Assets	2,699	730	3,429
Loan and advances at amortised cost (B3)	111,548	49,216	160,764
Loan commitments and financial guarantees (B10)	-	6,475	6,475
Debt securities at amortised cost	-	862	862
	114,247	57,283	171,530

B1 Cash and balances with Central Bank

31 December 2017 USD'000	31 December 2018 USD'000		31 December 2018 RO'000	31 December 2017 RO'000
43,774	**63,309**	Cash	**24,374**	16,853
1,312	**1,312**	Capital deposit with CBO	**505**	505
428,483	**123,576**	Balance with CBO	**47,577**	164,966
473,569	**188,197**		**72,456**	182,324

(i) The capital deposit with CBO cannot be withdrawn without its approval.

(ii) During the year, average minimum balance to be kept with CBO as statutory reserves is RO 72.42 million (2017: RO 62.47 million).

B2 Due from banks and other money market placements

31 December 2017 USD'000	31 December 2018 USD'000		31 December 2018 RO'000	31 December 2017 RO'000
		Local currency:		
-	**12,987**	Money market placements	**5,000**	-
-	**12,987**		**5,000**	-
		Foreign currency:		
132,177	**245,109**	Money market placements	**94,367**	50,888
58,506	**22,509**	Lending to banks	**8,666**	22,525
82,673	**35,875**	Demand balances	**13,812**	31,829
273,356	**303,493**		**116,845**	105,242
273,356	**316,480**		**121,845**	105,242
-	**(1,148)**	Expected credit loss allowance	**(442)**	-
(2,509)	-	Specific impairment allowance on lending to banks	-	(966)
(190)	-	Portfolio impairment allowance on lending to banks	-	(73)
270,657	**315,332**		**121,403**	104,203

B2 Due from banks and other money market placements (continued)

The analysis of changes in the ECL allowance on due from banks and other money market placements is as follows:

	31 December 2018 RO'000				31 December 2017 RO'000
	Stage 1	**Stage 2**	**Stage 3**	**Total**	
As at 1 January	**73**	**-**	**966**	**1,039**	148
Impact of adopting IFRS 9 (note A6.i)	**281**	**-**	**-**	**281**	-
As at 1 January 2018 (restated)	**354**	**-**	**966**	**1,320**	148
Net transfer between stages	**(78)**	**78**	**-**	**-**	-
Loan written off against ECL allowance	**-**	**-**	**(966)**	**(966)**	-
Net (release)/charge for the year (C6)	**(44)**	**132**	**-**	**88**	(75)
As at 31 December	**232**	**210**	**-**	**442**	73

	31 December 2018 USD'000				31 December 2017 USD'000
	Stage 1	**Stage 2**	**Stage 3**	**Total**	
As at 1 January	**190**	**-**	**2,509**	**2,699**	384
Impact of adopting IFRS 9 (note A6.i)	**730**	**-**	**-**	**730**	-
As at 1 January 2018 (restated)	**920**	**-**	**2,509**	**3,429**	-
Net transfer between stages	**(203)**	**203**	**-**	**-**	-
Loan written off against ECL allowance	**-**	**-**	**(2,509)**	**(2,509)**	-
Net (release)/charge for the year (C6)	**(114)**	**343**	**-**	**228**	(194)
As at 31 December 2018	**603**	**545**	**-**	**1,148**	190

The classification of due from banks and other money market placements based on the Bank's internal credit rating system and year-end stage classification are disclosed in note D.1.2 to the financial statements.

B3 Loans, advances and financing, net

31 December 2017 USD'000	31 December 2018 USD'000		31 December 2018 RO'000	31 December 2017 RO'000
3,846,990	**4,099,281**	Corporate	**1,578,223**	1,481,091
1,732,831	**1,980,355**	Retail	**762,437**	667,140
5,579,821	**6,079,636**	Gross loans, advances and financing	**2,340,660**	2,148,231
-	**(206,101)**	Expected credit loss allowance	**(79,349)**	-
(65,231)	**-**	Portfolio impairment allowance	**-**	(25,114)
(46,317)	**-**	Specific impairment allowance	**-**	(17,832)
(16,979)	**(24,366)**	Contractual interest not recognised	**(9,381)**	(6,537)
(128,527)	**(230,467)**		**(88,730)**	(49,483)
5,451,294	**5,849,169**	Net loans, advances and financing	**2,251,930**	2,098,748

Gross loans, advances and financing include RO 183.21 million (31 December 2017: RO 147.27 million) under Islamic mode of financing through Sohar Islamic financing activities.

B3 Loans, advances and financing, net (continued)

Loans, advances and financing comprise:

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
4,836,076	**5,327,545**	Loans	**2,051,105**	1,861,889
342,236	**332,260**	Overdrafts	**127,920**	131,761
281,130	**279,810**	Loans against trust receipts	**107,727**	108,235
120,379	**140,021**	Bills discounted	**53,908**	46,346
5,579,821	**6,079,636**	Gross loans, advances and financing	**2,340,660**	2,148,231
-	**(206,101)**	Expected credit loss allowance	**(79,349)**	-
(65,231)	**-**	Portfolio impairment allowance	**-**	(25,114)
(46,317)	**-**	Specific impairment allowance, including	**-**	(17,832)
(16,979)	**(24,366)**	contractual interest not recognised	**(9,381)**	(6,537)
(128,527)	**(230,467)**		**88,730**	49,483
5,451,294	**5,849,169**	Net loans, advances and financing	**2,251,930**	2,098,748

The below table provides a Comparison of provision held as per IFRS 9 and required as per CBO norms

CBO classification	IFRS 9 classification RO'000	Gross carrying amount RO'000	CBO Provision RO'000	IFRS 9 Provisions RO'000	Difference between CBO and IFRS 9 RO'000	Net carrying amount RO'000	IFRS 9 Reserve interest RO'000	CBO Reserve interest RO'000
(1)	(2)	(3)	(4)	(5)	(6)=(4)-(5)	(7)=(3)-(5)	(8)	(9)
Standard	Stage 1	1,825,031	22,231	12,685	9,546	1,812,346	-	-
	Stage 2	227,790	2,756	9,801	(7,045)	217,989	-	-
	Stage 3	199	2	81	(79)	118	-	-
Sub Total		**2,053,020**	**24,989**	**22,567**	**2,422**	**2,030,453**	**-**	-
Special mention	Stage 1	16	-	-	-	16	-	-
	Stage 2	209,849	10,951	23,791	(12,840)	186,058	-	-
	Stage 3	12	-	3	(3)	9	-	-
Sub Total		**209,877**	**10,951**	**23,794**	**(12,843)**	**186,083**	**-**	-
Substandard	Stage 1	99	-	1	(1)	98	-	-
	Stage 2	152	-	22	(22)	130	-	-
	Stage 3	12,001	2,984	3,464	(480)	8,537	275	275
Sub Total		**12,252**	**2,984**	**3,487**	**(503)**	**8,765**	**275**	**275**
Doubtful	Stage 1	227	-	3	(3)	224	-	-
	Stage 2	81	-	5	(5)	76	-	-
	Stage 3	21,625	10,754	10,821	(67)	10,804	417	417
Sub Total		**21,933**	**10,754**	**10,829**	**(75)**	**11,104**	**417**	**417**
Loss	Stage 1	375	-	6	(6)	369	-	-
	Stage 2	54	-	9	(10)	44	-	-
	Stage 3	43,149	23,475	18,656	4,819	24,493	8,689	8,689
Sub Total		**43,578**	**23,475**	**18,672**	**4,803**	**24,906**	**8,689**	**8,689**
Total	Stage 1	**1,825,748**	**22,231**	**12,695**	**9,536**	**1,813,053**	**-**	**-**
	Stage 2	**437,926**	**13,707**	**33,629**	**(19,922)**	**404,297**	**-**	**-**
	Stage 3	**76,986**	**37,215**	**33,025**	**4,190**	**43,961**	**9,381**	**9,381**
	Total	**2,340,660**	**73,153**	**79,349**	**(6,196)**	**2,261,311**	**9,381**	**9,381**

B3 Loans, advances and financing, net (continued)

CBO classification	IFRS 9 classification USD'000	Gross carrying amount USD'000	CBO Provision USD'000	IFRS 9 Provisions USD'000	Difference between CBO and IFRS 9 USD'000	Net carrying amount USD'000	IFRS 9 Reserve interest USD'000	CBO Reserve interest USD'000
(1)	(2)	(3)	(4)	(5)	(6)=(4)-(5)	(7)=(3)-(5)	(8)	(9)
Standard	Stage 1	4,740,340	57,743	32,948	24,795	4,707,392	-	-
	Stage 2	591,662	7,158	25,457	(18,299)	566,205	-	-
	Stage 3	517	5	210	(205)	306	-	3
Sub Total		**5,332,520**	**64,906**	**58,616**	**6,291**	**5,273,904**	-	**3**
Special mention	Stage 1	42	-	-	-	42	-	-
	Stage 2	545,062	28,444	61,795	(33,351)	483,268	-	-
	Stage 3	31	-	8	(8)	23	-	-
Sub Total		**545,135**	**28,444**	**61,803**	**(33,358)**	**483,332**	-	-
Substandard	Stage 1	257	-	3	(3)	255	-	-
	Stage 2	395	-	57	(57)	338	-	-
	Stage 3	31,171	7,751	8,997	(1,247)	22,174	714	714
Sub Total		**31,823**	**7,751**	**9,057**	**(1,306)**	**22,766**	**714**	**714**
Doubtful	Stage 1	590	-	8	(8)	582	-	-
	Stage 2	210	-	13	(13)	197	-	-
	Stage 3	56,169	27,932	28,106	(174)	28,062	1,083	1,083
Sub Total		**56,969**	**27,932**	**28,127**	**(195)**	**28,842**	**1,083**	**1,083**
Loss	Stage 1	974	-	16	(16)	958	-	-
	Stage 2	140	-	23	(26)	117	-	-
	Stage 3	112,075	60,974	48,457	12,517	63,618	22,569	22,569
Sub Total		**113,189**	**60,974**	**48,499**	**12,475**	**64,691**	**22,569**	**22,569**
Total	Stage 1	**4,742,203**	**57,743**	**32,974**	**24,769**	**4,709,229**	-	-
	Stage 2	**1,137,470**	**35,603**	**87,348**	**(51,745)**	**1,050,122**	-	-
	Stage 3	**199,964**	**96,662**	**85,779**	**10,883**	**114,184**	**24,366**	**24,366**
	Total	**6,079,636**	**190,008**	**206,101**	**(16,094)**	**5,873,535**	**24,366**	**24,366**

The analysis of changes in the gross carrying amount and corresponding ECL allowance on loans, advances and financing is as follows:

Gross carrying amount	**Stage 1 RO'000**	**Stage 2 RO'000**	**Stage 3 RO'000**	**Total RO'000**
As at 1 January 2018	**1,489,919**	**596,653**	**61,659**	**2,148,231**
New assets originated or purchased	698,847	140,630	8,169	**847,646**
Assets derecognised or repaid	(453,055)	(195,672)	(6,490)	**(655,217)**
Transfers to Stage 1	108,358	(107,027)	(1,331)	-
Transfers to Stage 2	(18,126)	20,655	(2,529)	-
Transfers to Stage 3	(192)	(17,313)	17,505	-
Amounts written off	-	-	-	-
Foreign exchange adjustments	-	-	-	-
At 31 December 2018	**1,825,751**	**437,926**	**76,983**	**2,340,660**

ECL	**Stage 1 RO'000**	**Stage 2 RO'000**	**Stage 3 RO'000**	**Total RO'000**
As at 1 January 2018 (Note A6 i)	-	-	-	**42,946**
Impact of adopting IFRS 9 (Note A6 i)	-	-	-	**18,948**
Restated ECL allowance as at 1 January 2018	**6,017**	**28,435**	**27,442**	**61,894**
Transfers to Stage 1	4,107	(3,573)	(534)	-
Transfers to Stage 2	(23)	1,138	(1,115)	-
Transfers to Stage 3	(12)	(635)	647	-
Net charge for the year (C6)	2,606	8,264	6,585	**17,455**
At 31 December 2018	**12,695**	**33,629**	**33,025**	**79,349**

B3 Loans, advances and financing, net (continued)

Gross carrying amount	**Stage 1** USD'000	**Stage 2** USD'000	**Stage 3** USD'000	**Total** USD'000
As at 1 January 2018	**3,869,919**	**1,549,748**	**160,153**	**5,579,821**
New assets originated or purchased	1,815,187	365,273	21,218	**2,201,678**
Assets derecognised or repaid	(1,176,766)	(508,239)	(16,857)	**(1,701,862)**
Transfers to Stage 1	281,449	(277,992)	(3,457)	-
Transfers to Stage 2	(47,081)	53,649	(6,569)	-
Transfers to Stage 3	(499)	(44,969)	45,468	-
Amounts written off	-	-	-	-
Foreign exchange adjustments	-	-	-	-
At 31 December 2018	**4,742,210**	**1,137,470**	**199,956**	**6,079,636**

ECL	**Stage 1** USD'000	**Stage 2** USD'000	**Stage 3** USD'000	**Total** USD'000
As at 1 January 2018 (Note A6 i)	-	-	-	**111,548**
Impact of adopting IFRS 9 (Note A6 i)	-	-	-	**49,215**
Restated ECL allowance as at 1 January 2018	**15,628**	**73,857**	**71,278**	**160,763**
Transfers to Stage 1	**10,668**	**(9,281)**	**(1,387)**	-
Transfers to Stage 2	**(60)**	**2,956**	**(2,896)**	-
Transfers to Stage 3	**(31)**	**(1,649)**	**1,680**	-
Net charge for the year (C6)	**6,769**	**21,465**	**17,104**	**45,338**
At 31 December 2018	**32,974**	**87,348**	**85,779**	**206,101**

The classification of loans, advances and financing, net, based on the Bank's internal credit rating system and year-end stage classification are disclosed in note D.1.2 to the financial statements.

Additional disclosures on NPL coverage as per BM 1149 is given below:

	As per CBO norms RO'000	**As per IFRS 9** RO'000	**Difference** RO'000
Impairment loss charged to profit and loss account	29,970	20,123	(9,847)
Provisions required as per CBO norms / held as per IFRS 9	82,579	94,780	12,201
Gross NPL ratio (percentage)*	3.26	3.29	**0.03**
Net NPL ratio (percentage)*	1.32	1.54	0.22

*NPL ratios are calculated on the basis of funded non-performing loans and advances.

B3 Loans, advances and financing, net (continued)

The movement in the impairment allowance per IAS 39 on loans, advances and financing is:

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
		Portfolio impairment allowance		
60,504	-	Balance at beginning of year	-	23,294
4,727	-	Provided during the year (note C6)	-	1,820
65,231	-	Balance at the end of the period (a)	-	25,114
		Specific impairment allowance		
		1) Loan loss provision		
33,566	-	Balance at beginning of year	-	12,923
45,197	-	Provided during the year	-	17,401
(26,974)	-	Written back due to recovery	-	(10,385)
(145)	-	Written off during the year	-	(56)
(5,327)	-	Transfer (to) / from memoranda accounts	-	(2,051)
46,317	-	Balance at the end of the year (b)	-	17,832
		2) Contractual interest not recognised		
13,535	**16,979**	Balance at beginning of year	**6,537**	5,211
7,784	**9,849**	Not recognised during the year	**3,792**	2,997
(3,686)	**(2,462)**	Written back due to recovery	**(948)**	(1,419)
(654)	-	Transfer to memoranda accounts	-	(252)
16,979	**24,366**	Balance at end of the year (c)	**9,381**	6,537
128,527	**24,366**	Total impairment (a) + (b) + (c)	**9,381**	49,483

The portfolio impairment allowance was established to meet credit risks inherent within loans, advances and financing at a portfolio level.

All loans and advances require payment of interest, some at fixed rates and others at rates that reprice prior to maturity. Interest reserve account is maintained to comply with rules; regulations and guidelines issued by CBO on loans, advances and financing that are impaired. As of 31 December 2018, loans and advances on which interest was not being accrued or where interest was reserved amounted to RO 76.986 million. (31 December 2017: RO 49.803 million)

Loans with renegotiated terms are defined as loans that have been restructured due to deterioration in the borrower's financial position, for which the Bank has made concessions by agreeing to terms and conditions that are more favourable for the borrower than the Bank had provided initially and that it would not otherwise consider. A loan continues to be presented as part of loans with renegotiated terms until maturity, early repayment or write-off.

CBO classification	**IFRS 9 classification RO'000**	**Gross carrying amount RO'000**	**CBO Provision RO'000**	**IFRS 9 Provisions RO'000**	**Difference between CBO and IFRS 9 RO'000**	**Net carrying amount RO'000**	**IFRS 9 Reserve interest RO'000**	**CBO Reserve interest RO'000**
(1)	(2)	(3)	(4)	(5)	(6)=(4)-(5)	(7)=(3)-(5)	(8)	(9)
Classified as performing	Stage 1	-	-	-	-	-	-	-
	Stage 2	55,972	8,396	9,515	(1,119)	46,457	-	-
	Stage 3	-	-	-	-	-	-	-
Total		**55,972**	**8,396**	**9,515**	**(1,119)**	**46,457**	-	-
Classified as non-performing	Stage 1	-	-	-	-	-	-	-
	Stage 2	-	-	-	-	-	-	-
	Stage 3	-	-	-	-	-	-	-
Total	Stage 1	-	-	-	-	-	-	-
	Stage 2	**55,972**	**8,396**	**9,515**	**(1,119)**	**46,457**	-	-
	Stage 3	-	-	-	-	-	-	-
	Total	**55,972**	**8,396**	**9,515**	**(1,119)**	**46,457**	-	-

CBO classification	IFRS 9 classification USD'000	Gross carrying amount USD'000	CBO Provision USD'000	IFRS 9 Provisions USD'000	Difference between CBO and IFRS 9 USD'000	Net carrying amount USD'000	IFRS 9 Reserve interest USD'000	CBO Reserve interest USD'000
(1)	(2)	(3)	(4)	(5)	(6)=(4)-(5)	(7)=(3)-(5)	(8)	(9)
Classified as performing	Stage 1	-	-	-	-	-	-	-
	Stage 2	145,382	21,808	24,714	(2,906)	120,668	-	-
	Stage 3	-	-	-	-	-	-	-
Total		**145,382**	**21,808**	**24,714**	**(2,906)**	**120,668**	**-**	**-**
Classified as non-performing	Stage 1	-	-	-	-	-	-	-
	Stage 2	-	-	-	-	-	-	-
	Stage 3	-	-	-	-	-	-	-
Total	Stage 1	-	-	-	-	-	-	-
	Stage 2	**145,382**	**21,808**	**24,714**	**(2,906)**	**120,668**	**-**	**-**
	Stage 3	-	-	-	-	-	-	-
	Total	**145,382**	**21,808**	**24,714**	**(2,906)**	**120,668**	**-**	**-**

B3 Loans, advances and financing, net (continued)

The below table analyses the concentration of gross loans and advances by economic sector:

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
1,732,831	**1,980,356**	Personal	**762,437**	667,140
1,067,390	**1,109,468**	Construction	**427,145**	410,945
654,605	**694,421**	Wholesale and retail	**267,352**	252,023
875,301	**955,117**	Services	**367,720**	336,991
155,730	**144,738**	Financial institutions	**55,724**	59,956
126,247	**101,283**	Transport and communication	**38,994**	48,605
398,153	**421,647**	Manufacturing	**162,334**	153,289
71,257	**128,904**	International trade	**49,628**	27,434
200,722	**226,278**	Mining and quarrying	**87,117**	77,278
172,894	**197,488**	Electricity, gas and water	**76,033**	66,564
99,553	**108,470**	Non – resident	**41,761**	38,328
17,686	**6,512**	Agriculture and allied activities	**2,507**	6,809
31	**-**	Government	**-**	12
7,421	**4,956**	Other	**1,908**	2,857
5,579,821	**6,079,636**		**2,340,660**	2,148,231

The analysis of changes in the ECL allowance on due from banks and other money market placements, loans, advances and financing (excluding contractual interest not recognised), investments and loan commitments and financial guarantees is as follows:

	Stage 1 RO'000	**Stage 2 RO'000**	**Stage 3 RO'000**	**Total RO'000**
As at 1 January 2018	**25,187**	**-**	**18,798**	**43,985**
Impact of adopting IFRS 9 (note A6.i)	(17,731)	29,147	10,638	**22,054**
As at 1 January 2018 (restated)	**7,456**	**29,147**	**29,436**	**66,039**
Transfers to Stage 1	4,283	(3,749)	(3,457)	-
Transfers to Stage 2	(266)	1,381	(6,569)	-
Transfers to Stage 3	(12)	(636)	45,468	-
Net charge for the year	4,439	10,321	5,566	**20,326**
Written off during the year	-	-	(966)	**(966)**
At 31 December 2018	**15,900**	**36,464**	**33,035**	**85,399**

B4 Investment securities

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
-	**256,083**	Held at FVTPL	**98,592**	-
-	**761,107**	Held at FVOCI	**293,026**	-
-	**366,626**	Held at amortised cost	**141,151**	-
287,532	-	Held for trading investments	-	110,700
554,168	-	Available for sale investments	-	213,355
232,952	-	Held to maturity investments	-	89,686
1,074,652	**1,383,816**		**532,769**	413,741

B4.a Held at FVTPL (2017: Held for trading investments):

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
273,693	**224,078**	Government development bonds – Oman	**86,270**	105,372
13,839	**21,036**	Sukuk trust certificates – secured	**8,099**	5,328
-	**6,494**	Unquoted securities	**2,500**	-
-	**4,475**	Others	**1,723**	-
287,532	**256,083**	**Total**	**98,592**	110,700

B4 Investment securities

B4.b Held at FVOCI (2017: Available for sale investments):

	Carrying / fair value 31 December 2018	Cost 31 December 2018	Carrying / fair value 31 December 2017	Cost 31 December 2017
	RO'000	RO'000	RO'000	RO'000
Unquoted securities	-	34	2,254	2,288
Quoted securities	18,909	21,022	26,051	29,672
Treasury bills	274,117	273,350	185,050	185,313
	293,026	294,406	213,355	217,273

	Carrying/ fair value 31 December 2018	Cost 31 December 2018	Carrying/ fair value 31 December 2017	Cost 31 December 2017
	USD'000	USD'000	USD'000	USD'000
Unquoted securities	-	88	5,854	5,943
Quoted securities	49,115	54,603	67,665	77,070
Treasury bills	711,992	710,000	480,649	481,332
	761,107	764,691	554,168	564,345

- As at 31 December 2017, unquoted securities includes an investment of RO 2.25 million in the Oman Development Fund SAOC ("Fund"). As at 1 January 2018, they were reclassified to investments held at FVTPL. The Fund was incorporated on 7 May 2014 under license no. 1196427 with the Bank being the founder shareholder. The purpose of the Fund is to identify mid-segment industrial and manufacturing sectors that leverage Oman's unique advantages such as its infrastructure, tax treaties, geography and natural mineral resources for potential investment opportunities. During the year the Bank invested RO 245,599 in line with the other investors in the fund. The Bank currently holds a 12.66% stake in the Fund (31 December 2017: 16.9%). The Bank has an Investment Management Agreement with the Fund.

- ECL allowance on treasury bills as of 31 December 2018 amounted to RO 0.02 million (31 December 2017 (opening transition adjustment): RO 0.02 million). This adjustment is reflected in the other comprehensive income.

- Treasury bills include investments in USD Treasury bills of RO 273.35 million (31 December 2017: RO 184.80 million) assigned as collaterals against the Bank's borrowings.

- In 2018, the Bank received dividends of RO 1.18 million from its FVOCI equities (2017: RO 0.7 million for available-for-sale securities), recorded as other operating income.

- The Bank has designated its equity investments previously classified as available-for-sale as equity investments at FVOCI on the basis that these are not held for trading.

- The fair value of the Bank's debt instruments measured at FVOCI by credit risk, based on the Bank's internal credit rating system and year-end stage classification are disclosed in note D.1.2 to the financial statements.

- The credit rating profile of investment debt securities has been disclosed in note D.1.3 to the financial statements.

- FVOCI includes investment in debt securities amounting to RO 290.2 million and investment in equity securities amounting to RO 2.82 million respectively.

B4 Investment securities

B4.c Held at amortised cost (2017: Held to maturity):

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
225,077	**369,213**	Quoted	**142,147**	86,654
7,875	**-**	Unquoted	**-**	3,032
232,952	**369,213**		**142,147**	89,686
-	**(2,587)**	Expected credit loss allowance	**(996)**	-
232,952	**366,626**	**Total**	**141,151**	89,686

The analysis of changes in the fair value and the corresponding ECL allowance on debt investments classified as held at amortised cost is as follows:

	Stage 1 RO'000	Stage 2 RO'000	Stage 3 RO'000	Total RO'000
Balance as at 1 January 2018	**91750**	**-**	**-**	**91,750**
New assets originated or purchased	**50,397**	**-**	**-**	**50,397**
Assets derecognised or matured (exlcuding write offs)	**-**	**-**	**-**	**-**
Change in fair value	**-**	**-**	**-**	**-**
Transfers to Stage 1	**(24,047)**	**24,047**	**-**	**-**
Transfers to Stage 2	**-**	**-**	**-**	**-**
Transfers to Stage 3	**-**	**-**	**-**	**-**
Amounts written off	**-**	**-**	**-**	**-**
Foreign exchange adjustments	**-**	**-**	**-**	**-**
At 31 December 2018	**118,100**	**24,047**	**-**	**142,147**

	Stage 1 RO'000	Stage 2 RO'000	Stage 3 RO'000	Total RO'000
Balance as at 1 January 2018	**-**	**-**	**-**	**-**
Impact of adopting IFRS 9 (Note A6 i)	**332**	**-**	**-**	**332**
Restated ECL allowance as at 1 January 2018	**332**	**-**	**-**	**332**
Transfers to Stage 1	**-**	**-**	**-**	**-**
Transfers to Stage 2	**(165)**	**165**	**-**	**-**
Transfers to Stage 3	**-**	**-**	**-**	**-**
Net charge for the year (C6)	**152**	**512**	**-**	**664**
At 31 December 2018	**319**	**677**	**-**	**996**

B4 Investment securities (continued)

B4.c Held at amortised cost (2017: Held to maturity) (continued)

	Stage 1 USD'000	Stage 2 USD'000	Stage 3 USD'000	Total USD'000
Balance as at 1 January 2018	**238,312**	**-**	**-**	**238,312**
New assets originated or purchased	**130,901**	**-**	**-**	**130,901**
Assets derecognised or matured (exlcuding write offs)	**-**	**-**	**-**	**-**
Change in fair value	**-**	**-**	**-**	**-**
Transfers to Stage 1	**(62,460)**	**62,460**	**-**	**-**
Transfers to Stage 2	**-**	**-**	**-**	**-**
Transfers to Stage 3	**-**	**-**	**-**	**-**
Amounts written off	**-**	**-**	**-**	**-**
Foreign exchange adjustments	**-**	**-**	**-**	**-**
At 31 December 2018	**306,753**	**62,460**	**-**	**369,213**

	Stage 1 USD'000	Stage 2 USD'000	Stage 3 USD'000	Total USD'000
Balance as at 1 January 2018	**-**	**-**	**-**	**-**
Impact of adopting IFRS 9 (note A6 i)	**862**	**-**	**-**	**862**
Restated ECL allowance as at 1 January 2018	**862**	**-**	**-**	**862**
Transfers to Stage 1	**-**	**-**	**-**	**-**
Transfers to Stage 2	**(429)**	**429**	**-**	**-**
Transfers to Stage 3	**-**	**-**	**-**	**-**
Net charge for the year (C6)	**395**	**1,330**	**-**	**1,725**
At 31 December 2018	**828**	**1,759**	**-**	**2,587**

B5 Property, equipment and fixtures

	Freehold land RO'000	Computer software RO'000	Furniture and fixtures RO'000	Office equipment RO'000	Motor vehicles RO'000	Capital work –in-progress RO'000	Total RO'000
Cost:							
1 January 2018	**4,100**	**15,307**	**5,174**	**6,368**	**822**	**2,076**	**33,847**
Additions	**-**	**1,051**	**364**	**747**	**107**	**3,678**	**5,947**
Transfers/ disposals	**-**	**865**	**(72)**	**(72)**	**-**	**(865)**	**(144)**
Written off (C5)	**-**	**-**	**-**	**-**	**-**	**(1,100)**	**(1,100)**
As at 31 December 2018	**4,100**	**17,223**	**5,466**	**7,043**	**929**	**3,789**	**38,550**
Accumulated depreciation:							
1 January 2018	**-**	**7,209**	**3,929**	**4,929**	**671**	**-**	**16,738**
Depreciation	**-**	**1,312**	**393**	**489**	**79**	**-**	**2,273**
Disposals	**-**	**-**	**(66)**	**(71)**	**-**	**-**	**(137)**
As at 31 December 2018	**-**	**8,521**	**4,256**	**5,347**	**750**	**-**	**18,874**
Net book value at							
31 December 2018 (RO'000)	**4,100**	**8,702**	**1,210**	**1,696**	**179**	**3,789**	**19,676**
31 December 2018 (USD'000)	**10,649**	**22,603**	**3,143**	**4,405**	**465**	**9,842**	**51,107**

i) During 2018, design cost amounting to RO 1.1 million previously capitalised, and no longer associated with the underlying project have been written off.

ii) Included in capital work in progress are costs incurred towards a new head office project.

iii) During the year 2017, staff costs amounting to RO 384 thousand towards upgrade of core banking system were capitalised under computer software

	Freehold land RO'000	Computer software RO'000	Furniture and fixtures RO'000	Office equipment RO'000	Motor vehicles RO'000	Capital work-in-progress RO'000	Total RO'000
Cost:							
At 1 January 2017	4,100	10,864	4,966	5,895	822	3,769	30,416
Additions	-	2,146	208	473	-	604	3,431
Disposals	-	2,297	-	-	-	(2,297)	-
At 31 December 2017	4,100	15,307	5,174	6,368	822	2,076	33,847
Accumulated depreciation:							
At 1 January 2017	-	(6,171)	(3,480)	(4,459)	(582)	-	(14,692)
Depreciation	-	(1,038)	(449)	(470)	(89)	-	(2,046)
Disposals	-	-	-	-	-	-	-
As at 31 December 2017	-	(7,209)	(3,929)	(4,929)	(671)	-	(16,738)
Net book value at							
31 December 2017 (RO'000)	4,100	8,098	1,245	1,439	151	2,076	17,109
31 December 2017 (USD'000)	10,649	21,034	3,234	3,738	392	5,392	44,439

B6 Investment properties

Investment properties represent two plots of land received by the Bank as grant from the Government of Sultanate of Oman during the year 2008. The Bank has recorded the land based on the average valuation carried out during 2008 by two professional valuators. The plots of land are currently held vacant. The fair value of these properties as at 31 December 2018 is RO 3.0 million (31 December 2017: RO 3.0 million).

As at 31 December 2018 and 2017, the fair values of the properties are based on valuations performed by an accredited independent valuer. The valuation was conducted on an open market basis. These properties have been classified as level 3 investments.

B7 Other assets

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
255,77	**78,577**	Acceptances (i)	**30,252**	9,847
5,753	**5,730**	Prepayments	**2,206**	2,215
10,447	**3,839**	Receivables	**1,478**	4,022
4,530	**4,891**	Positive fair value of derivatives (B24)	**1,883**	1,744
15,493	**24,545**	Others	**9,450**	5,965
61,800	**117,582**		**45,269**	23,793

(i) Disclosure on ECL on acceptances is at B10(i).

B8 Due to banks and other money market borrowings

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
		Local currency:		
104,412	**25,977**	Money market borrowings	**10,001**	40,199
83,494	**12,816**	Demand balances	**4,934**	32,145
187,906	**38,793**		**14,935**	72,344
		Foreign currency:		
876,894	**1,033,309**	Money market borrowings	**397,824**	337,604
140	**306**	Demand balances	**118**	54
801,603	**803,075**	Syndicated borrowings	**309,184**	308,617
1,678,637	**1,836,690**		**707,126**	646,275
1,866,543	**1,875,483**		**722,061**	718,619

Foreign currency borrowings include bank borrowings amounting to RO 296.45 million (2017: RO 200.20 million) with underlying collaterals in the form of USD Treasury bills of RO 273.35 million (2017: RO 184.88 million)

Applicable financial covenants for the syndicated borrowings include the requirement for a minimum tangible net worth of the Bank and a minimum capital adequacy ratio to be maintained by the Bank.

B9 Customers' deposits

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
2,445,860	**2,635,782**	Term deposits	**1,014,776**	941,656
1,050,930	**1,321,065**	Demand deposits	**508,610**	404,608
726,613	**718,244**	Saving deposits	**276,524**	279,746
43,727	**47,904**	Margin deposits	**18,443**	16,835
4,267,130	**4,722,995**		**1,818,353**	1,642,845

	31 December 2018			31 December 2017		
	Conventional banking RO'000	**Islamic banking RO'000**	**Total RO'000**	Conventional banking RO'000	Islamic banking RO'000	Total RO'000
Retail customers:						
Term deposits	**80,196**	**15,547**	**95,743**	69,034	11,496	80,530
Demand deposits	**22,706**	**3,799**	**26,505**	19,555	3,203	22,758
Saving deposits	**235,787**	**25,497**	**261,284**	245,579	12,366	257,945
Corporate customers:						
Term deposits	**813,660**	**105,373**	**919,033**	763,861	97,265	861,126
Demand deposits	**474,647**	**7,458**	**482,105**	374,993	6,857	381,850
Saving deposits	**-**	**15,240**	**15,240**	-	21,801	21,801
Margin deposits	**10,532**	**7,911**	**18,443**	7,059	9,776	16,835
Total	**1,637,528**	**180,825**	**1,818,353**	1,480,081	162,764	1,642,845

	31 December 2018			31 December 2017		
	Conventional banking USD'000	**Islamic banking USD'000**	**Total USD'000**	Conventional banking USD'000	Islamic banking USD'000	Total USD'000
Retail customers:						
Term deposits	**208,301**	**40,382**	**248,683**	179,309	29,860	209,169
Demand deposits	**58,977**	**9,868**	**68,845**	50,793	8,319	59,112
Saving deposits	**612,434**	**66,226**	**678,660**	637,868	32,119	669,987
Corporate customers:						
Term deposits	**2,113,403**	**273,696**	**2,387,099**	1,984,055	252,636	2,236,691
Demand deposits	**1,232,849**	**19,371**	**1,252,220**	974,008	17,810	991,818
Saving deposits	**-**	**39,584**	**39,584**	-	56,626	56,626
Margin deposits	**27,356**	**20,548**	**47,904**	18,335	25,392	43,727
Total	**4,253,320**	**469,675**	**4,722,995**	3,844,368	422,762	4,267,130

B10 Other liabilities

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
25,577	**78,577**	Acceptances	**30,252**	9,847
8,166	**9,587**	Staff entitlements	**3,691**	3,144
10,771	**12,956**	Income tax payable	**4,988**	4,147
2,332	**9,616**	Negative fair value of derivatives (B25)	**3,702**	898
738	**1,255**	Deferred tax liabilities	**483**	284
34,108	**95,937**	Other accruals and provisions	**36,936**	13,131
-	**11,979**	Expected credit loss allowance on loan commitments and financial guarantees	**4,612**	-
81,692	**219,907**	**Total**	**84,664**	31,451
		Staff entitlements:		
1,717	**1,416**	End of service benefits	**545**	661
6,449	**8,171**	Other liabilities	**3,146**	2,483
8,166	**9,587**		**3,691**	3,144
		Movement in the end of service benefits liability		
1,577	**1,717**	At 1 January	**661**	607
421	**354**	Expenses recognised in the profit or loss	**136**	162
(281)	**(655)**	End of service benefits paid	**(252)**	(108)
1,717	**1,416**		**545**	661

(i) The analysis of changes in the gross carrying amount and corresponding ECL allowance on loan commitments and financial guarantees is as follows:

Outstanding exposure	**Stage 1 RO'000**	**Stage 2 RO'000**	**Stage 3 RO'000**	**Total RO'000**
Balance as at 1 January 2018	**609,501**	**174,784**	**1,944**	**786,229**
New exposures	335,635	34,439	87	**370,161**
Exposure derecognised or matured/ lapsed (excluding write offs)	(354,146)	(66,442)	(2,887)	**(423,475)**
Transfers to Stage 1	35,435	(35,424)	(11)	-
Transfers to Stage 2	-	-	-	-
Transfers to Stage 3	-	(2,513)	2,513	-
Amounts written off				
Foreign exchange adjustments				
At 31 December 2018	**626,425**	**104,844**	**1,646**	**732,915**

ECL	**Stage 1 RO'000**	**Stage 2 RO'000**	**Stage 3 RO'000**	**Total RO'000**
Balance as at 1 January 2018	-	-	-	-
Impact of adopting IFRS 9 (Note A6 i)	**753**	**712**	**1,028**	**2,493**
Restated ECL allowance as at 1 January 2018	**753**	**712**	**1,028**	**2,493**
Transfers to Stage 1	**176**	**(176)**	-	-
Transfers to Stage 2	-	-	-	-
Transfers to Stage 3	-	**(1)**	**1**	-
Net charge for the year (C6)	**1,725**	**1,413**	**(1,019)**	**2,119**
At 31 December 2018	**2,654**	**1,948**	**10**	**4,612**

B10 Other liabilities (continued)

Outstanding exposure	Stage 1 USD'000	Stage 2 USD'000	Stage 3 USD'000	Total USD'000
Balance as at 1 January 2018	**1,583,119**	**453,984**	**5,050**	**2,042,153**
New exposures	871,779	89,452	226	961,457
Exposure derecognised or matured/ lapsed (excluding write offs)	(919,859)	(172,577)	(7,499)	(1,099,935)
Transfers to Stage 1	92,039	(92,010)	(29)	-
Transfers to Stage 2	-	-	-	-
Transfers to Stage 3	-	(6,527)	6,527	-
Amounts written off	-	-	-	-
Foreign exchange adjustments	-	-	-	-
At 31 December 2018	**1,627,078**	**272,322**	**4,275**	**1,903,675**

	Stage 1 USD'000	Stage 2 USD'000	Stage 3 USD'000	Total USD'000
Balance as at the beginning of the year	-	-	-	-
Impact of adopting IFRS 9 (Note A6 i)	**1,956**	**1,849**	**2,670**	**6,475**
Restated ECL allowance as at 1 January 2018	**1,956**	**1,849**	**2,670**	**6,475**
Transfers to Stage 1	**456**	**(456)**	-	-
Transfers to Stage 2	-	-	-	-
Transfers to Stage 3	-	**(3)**	**3**	-
Net charge for the year (C6)	**4,481**	**3,670**	**(2,647)**	**5,504**
At 31 December 2018	**6,893**	**5,060**	**26**	**11,979**

The classification of loan commitments and financial guarantees based on the Bank's internal credit rating system and year-end stage classification are disclosed in note D.1.2 to the financial statements.

B11 Subordinated loans

The Bank had raised unsecured subordinated loans of RO 50 million during the year 2010 with a maturity of 7 years. These subordinated loans were unlisted, non-transferable, non-negotiable and non-convertible with no early call option and carried a fixed rate of interest. The Bank was required to create a subordinated loan reserve equal to 20% of the issue value annually during the last five years of the term of the subordinated loans. As of 31 December 2016, a cumulative amount of RO 50 million was transferred to this reserve from retained earnings. During the year 2017, these subordinated loans were were fully paid off by the Bank and the subordinated loan reserve of RO 50 million was released back to retained earnings.

The Bank had further raised unsecured subordinated loans of RO 35 million during the year 2016 with a maturity of 7 years. These instruments are also unlisted, non-transferable, non-negotiable and non-convertible with no early call option and carries a fixed rate of interest. The principal amount of the subordinated loans is repayable on maturity i.e. in 2023 while interest is payable semi-annually. The Bank is required to create a subordinated loan reserve equal to 20% of the issue value annually during the last five years of the term of the subordinated loans. This reserve is created at the end of each financial year from retained earnings. Accordingly, during the year 2018 a reserve of RO 7.0 million (2017: RO nil) was created. The outstanding of this subordinated loan with accrued interest as of 31 December 2018 stands at RO 35.392 million (2017: RO 35.392 million).

According to the Regulations of CBO, the amount of subordinated loans as reduced by subordinated loan reserve is considered as Tier II capital for capital adequacy purposes.

B12 Compulsorily convertible bonds

Compulsorily convertible bonds of RO 7.150 million carrying an annual coupon rate of 4.5% were issued on 28 April 2013 as part of a dividend distribution. These bonds had to be converted into ordinary shares of the Bank in three equal instalments at the end of 3rd, 4th and 5th years from the date of issuance at a conversion price derived by applying a discount of 20% to the 3 months average share price of the Bank on the Muscat Securities Market prior to the date of conversion. Accordingly during 2016, 2017 and 2018 one-third of these bonds, amounting to RO 2.38 million each year were converted into ordinary shares of the Bank. The last instalment was converted on 28 April 2018 resulting in full conversion with NIL outstanding balance as at 31 December 2018 (31 December 2017: RO 2.402 million)

B13 Certificate of Deposits

The Certificates of Deposits issued in 2015 of RO 18 million were matured in 2018. The current outstanding balance of RO 509 thousands of accrued interest as of 31 December 2018 relates to Certificate of Deposits that were issued in 2016 with a maturity of five years. These are unsecured, denominated in Rial Omani and carries a fixed interest rate.

B14 Share capital and Share premium

The authorised share capital of the Bank is 4,000,000,000 shares of RO 0.100 each (31 December 2017: 2,000,000,000 of RO 0.100 each). The issued and paid up share capital of the Bank is 1,982,646,391 shares of RO 0.100 each (31 December 2017: 1,784,646,242 shares of RO 0.100 each).

At the Extraordinary General Meeting and Annual General Meeting held on 29 March 2018, the shareholders approved the Board's recommendation to increase the Bank's authorised share capital from 2,000,000,000 shares of RO 0.100 each to 4,000,000,000 shares of RO 0.100 each and to distribute bonus shares equal to 10% of issued and paid up share capital as at 31 December 2017, resulting in the issuance of 178,464,624 new shares in March 2018.

During April 2018, the remaining portion of compulsorily convertible bonds outstanding as of 31 December 2017 was converted into ordinary shares of the Bank resulting in issuance of 19,535,525 shares (2017: 19,696,967 shares) amounting to RO 1.95 million (2017: RO 1.97 million). The balance of RO 430 thousand (31 December 2017: 414 thousand) was credited to share premium account.

As of 31 December 2018, the following shareholders held 10% or more of the Bank's capital, either individually or together with related parties:

	Number of shares	*% Holding*
Oman Investment & Finance Co. SAOG	**304,714,636**	**15.37**
The Royal Court of Affairs	**288,852,420**	**14.57**

B14.a Proposed dividend

For the year 2018, the Board of Directors have proposed a cash dividend of 6 % of the share capital i.e., 6 baizas per share amounting to RO 11,895,900 (31 December 2017: cash dividend of 5% of the share capital i.e., 5 baizas per share amounting to RO 8,923,250 and bonus shares of 10% of the share capital, (i.e.10 shares for every 100 shares held) amounting to RO 17,846,500). The proposed dividend is subject to formal approval of the shareholders at the Annual General Meeting.

B15 Legal reserve

In accordance with the Commercial Companies Law of Oman of 1974, an annual appropriation of 10% of the profit for the year is required to be made to legal reserve until such time that the accumulated reserve is equal to at least one third of the Bank's issued share capital.

B16 General reserve

General reserve of RO 988,000 (31 December 2017: RO 988,000) was created to cover the losses incurred by Sohar Islamic window for the year 2013 and 2014. It commenced reporting profits from 2015 and accordingly; no further transfer was made post 2014.

B17 Special Reserve

As required by CBO circular BSD/2017/BKUP/Banks & FLCs/467, the Bank reserved 10% of the outstanding exposure of restructured facilities that are not classified as non-performing loans as of 31 December 2017. This reserve was transferred to the retained earnings with the implementation of IFRS 9.

B18 Fair value reserve

The fair value reserve includes the cumulative net change in the fair value of the investment securities held as FVOCI net of applicable income tax until the investment is derecognised, sold or impaired.

B19 Perpetual Tier 1 Capital Securities

The Bank issued Perpetual Tier 1 Capital Securities amounting to RO 100 million on 25 September 2017. The securities constitute direct, unconditional, subordinated and unsecured obligations of the Bank and are classified as equity in accordance with IAS 32: Financial Instruments – Classification. They do not have a fixed or final maturity date. The Bank may at its discretion and after prior consent from the relevant regulatory authority, exercise its option to redeem the securities in full (not in part) on the first Call Date , i.e the 5th anniversary of the Issue Date, and on every fifth anniversary thereafter, again subject to the prior consent of the regulatory authorities.

The Tier 1 Capital Securities bear interest on their nominal amount from the issue date to the first call date at a fixed annual rate of 7.75%. Thereafter the interest rate will reset at five year intervals. Interest will be payable semi-annually in arrears and treated as a deduction from equity. The Bank at its sole discretion may elect not to distribute interest. This is not considered as an event of default. If the Bank does not pay interest, on a scheduled interest payment date (for whatever reason), it cannot make any other distribution or payment on or with respect to its ordinary shares or any of its other Common Equity Tier 1 Instruments or securities, ranking junior to or pari passu with the Tier 1 Capital Securities unless and until it has paid one interest payment in full on the Tier 1 Capital Securities. The Tier 1 Capital Securities also allow the Bank to write-down (in whole or in part) any amounts due to the holders of the Securities under certain circumstances.

RO 7.750 million was paid as coupon during 2018 and is recognised in the statement of changes in equity.

B20 Net assets per share

The calculation of net assets per share is based on net assets of RO 285.42 million as at 31 December 2018 (31 December 2017: RO 293.60 million) attributable to ordinary shareholders of 1,982,646,391 ordinary shares (31 December 2017: 1,784,646,242 ordinary shares),being the number of shares outstanding as at 31 December 2018.

B21 Contingent liabilities and commitments

B21.a Contingent liabilities

Standby letters of credit and guarantees commit the Bank to make payments on behalf of customers, contingent upon the failure of the customer to perform under the terms of a specified contract.

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
978,138	**984,512**	Guarantees	**379,037**	376,583
206,545	**275,597**	Documentary letters of credit	**106,105**	79,520
1,184,683	**1,260,109**		**485,142**	456,103

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
726,777	**715,003**	Construction	**275,276**	279,809
168,831	**255,538**	Financial institution	**98,382**	65,000
67,888	**99,049**	International trade	**38,134**	26,137
111,281	**91,340**	Services	**35,166**	42,843
50,844	**35,849**	Manufacturing	**13,802**	19,575
8,296	**21,730**	Government	**8,366**	3,194
13,613	**11,761**	Transport and communication	**4,528**	5,241
1,766	**434**	Mining and quarrying	**167**	680
28,558	**23,522**	Electricity, gas and water	**9,056**	10,995
6,829	**5,883**	Others	**2,265**	2,629
1,184,683	**1,260,109**		**485,142**	456,103

B21.b Commitments

Credit related commitments include commitments to extend credit, standby letters of credit and guarantees that are designed to meet the requirements of the Bank's customers. Commitments to extend credit represent contractual commitments to make loans and revolving credits. Commitments generally have fixed expiry dates or other termination clauses and require the payment of a fee. Since commitments may expire without being drawn upon, the total contracted amounts do not necessarily represent future cash obligations.

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
1,340	**4,306**	Capital commitments	**1,658**	516
723,242	**1,136,847**	Credit related commitments	**437,686**	278,448
724,582	**1,141,153**		**439,344**	278,964

B21 Contingent liabilities and commitments (continued)

B21.c Litigation

Litigation is a common occurrence in the Banking industry due to the nature of the business it undertakes. The Bank has formal controls and policies for managing legal claims. Once professional advice has been obtained and the amount of loss reasonably estimated, the Bank makes provides for any adverse effects that the claims may have on its financial standing. No provision (2017:None) has been made as at 31 December 2018, as professional advice indicates that it is unlikely that any significant loss will arise.

B22 Related party transactions

In the ordinary course of business the Bank enters into transactions with certain of its directors, shareholders, senior management, Shari'a supervisory board, Shari'a reviewer and companies in which they have a significant interest. These transactions are conducted on an arm's length basis and are approved by the Bank's management and Board of Directors.

The aggregate amount of balances and the income and expenses generated with such related parties are as follows:

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
		Key management personnel		
6,906	**6,052**	Loans, advances and financing at the end of year	**2,330**	2,659
1,532	**429**	Loans disbursed during the year	**165**	590
(1,701)	**(790)**	Loans repaid during the year	**(304)**	(655)
1,883	**2,558**	Deposits at the end of the year	**985**	725
3,501	**1,065**	Deposits received during the year	**410**	1,348
(3,117)	**(348)**	Deposits paid during the year	**(134)**	(1,200)
345	**257**	Interest income during the year	**99**	133
		Other related parties		
15,995	**218,332**	Loans, advances and financing at the end of year	**84,058**	6,158
44,041	**227,412**	Loans disbursed during the year	**87,554**	16,956
(36,914)	**(11,590)**	Loans repaid during the year	**(4,462)**	(14,212)
26,404	**20,684**	Deposits at the end of the year	**7,963**	10,165
29,200	**21,317**	Deposits received during the year	**8,207**	11,242
(35,226)	**(9,405)**	Deposits paid during the year	**(3,621)**	(13,562)
971	**6,247**	Interest income during the year	**2,405**	374
1,444	**125**	Interest expense during the year	**48**	556
		Key management personnels' compensation		
7,732	**10,771**	Salaries and other short term benefits	**4,147**	2,977
249	**553**	Post-employment benefits	**213**	96
517	**478**	Directors' sitting fees and remuneration	**184**	199
114	**130**	Shari'a Supervisory Board members	**50**	44

B22 Related party transactions (continued)

The aggregate amount of balances and the income and expenses generated with shareholders holding 10% or more of the Banks' shares are as follows:

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
-	**10,390**	Loans, advances and financing at the end of year	**4,000**	-
14,494	**10,390**	Loans disbursed during the year	**4,000**	5,580
(61,727)	**-**	Loans repaid during the year	**-**	(23,765)
3,278	**6,221**	Deposits at the end of the year	**2,395**	1,262
47	**5,218**	Deposits received during the year	**2,009**	18
(11,304)	**(2,273)**	Deposits paid during the year	**(875)**	(4,352)
161	**109**	Interest income during the year	**42**	62
36	**31**	Interest expense during the year	**12**	14

As at 31 December 2018, no loans to related parties are classified under stage 3 (31 December 2017: nil)

B23 Fair value of financial instruments

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

i) In the accessible principal market for the asset or liability; or
ii) In the absence of a principal market, in the most advantageous accessible market for the asset or liability.

The Bank uses the following hierarchy for determining and disclosing the fair value of financial instruments:

Level 1: quoted prices in active markets for the same instrument (i.e., without modification or repacking);
Level 2: quoted prices in active markets for similar assets and liabilities or other valuation techniques for which all significant inputs are based on observable market data; and
Level 3: valuation techniques for which any significant input is not based on observable market data.

The Bank considers that the fair value of financial instruments was not significantly different to their carrying value (including accrued interest) at each of those dates. The table below sets out the classification and fair value of each class of financial assets and liabilities:

B23 Fair value of financial instruments (continued)

At 31 December 2018	Amortised cost	FVOCI	FVTPL	Total carrying (including accrued interest)/fair value
Assets				
Cash and balances with Central Bank	72,456	-	-	72,456
Due from banks and other money market placements	121,403	-	-	121,403
Loans, advances and financing	2,251,930	-	-	2,251,930
Investments	141,151	293,026	98,592	532,769
Other assets (excluding prepayments)	43,063	-	-	43,063
Total	2,630,003	293,026	98,592	3,021,621
Liabilities				
Due to banks and other money market borrowings				722,061
Customers' deposits				1,818,353
Other liabilities (excluding other accruals & provisions)				47,728
Subordinated loans				35,392
Certificates of deposits				509
Total				2,624,043

At 31 December 2017	Loans and receivables RO'000	Held to maturity RO'000	Available for sale RO'000	Held for trading RO'000	Total carrying (including accrued interest)/fair value RO'000
Assets					
Cash and balances with Central Bank	182,324	-	-	-	182,324
Due from banks and other money market placements	104,203	-	-	-	104,203
Loans, advances and financing	2,098,748	-	-	-	2,098,748
Investments	-	89,686	213,355	110,700	413,741
Other assets (excluding prepayments)	21,578	-	-	-	21,578
Total	2,406,853	89,686	213,355	110,700	2,820,594
Liabilities					
Due to banks and other money market borrowings					718,619
Customers' deposits					1,642,845
Other liabilities (excluding other accruals & provisions)					18,320
Subordinated loans					35,392
Compulsorily convertible bonds					2,402
Certificates of deposits					18,513
Total					2,436,091

B23 Fair value of financial instruments (continued)

At 31 December 2018	Amortised cost USD'000	FVOCI USD'000	FVTPL USD'000	Total carrying (including accrued interest)/fair value USD'000
Assets				
Cash and balances with Central Bank	**188,197**	**-**	**-**	**188,197**
Due from banks and other money market placements	**315,332**	**-**	**-**	**315,332**
Loans, advances and financing	**5,849,169**	**-**	**-**	**5,849,169**
Investments	**366,626**	**761,107**	**256,083**	**1,383,816**
Other assets (excluding prepayments)	**111,852**	**-**	**-**	**111,852**
Total	**6,831,176**	**761,107**	**256,083**	**7,848,366**
Liabilities				
Due to banks and other money market borrowings				**1,875,483**
Customers' deposits				**4,722,995**
Other liabilities (excluding other accruals & provisions)				**123,969**
Subordinated loans				**91,927**
Certificates of deposits				**1,322**
Total				**6,815,696**

At 31 December 2017	Loans and receivables USD'000	Held to maturity USD'000	Available for sale USD'000	Held for trading USD'000	Total carrying (including accrued interest)/fair value USD'000
Assets					
Cash and balances with Central Bank	473,569	-	-	-	473,569
Due from banks and other money market placements	270,657	-	-	-	270,657
Loans, advances and financing	5,451,294	-	-	-	5,451,294
Investments	-	232,952	554,168	287,532	1,074,652
Other assets (excluding prepayments)	56,047	-	-	-	56,047
Total	6,251,567	232,952	554,168	287,532	7,326,219
Liabilities					
Due to banks and other money market borrowings					1,866,543
Customers' deposits					4,267,130
Other liabilities (excluding other accruals & provisions)					47,584
Subordinated loans					91,927
Compulsorily convertible bonds					6,239
Certificates of deposits					48,086
Total					6,327,509

B23 Fair value of financial instruments (continued)

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 carried at amortised cost and derivatives

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

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

Bank and customer deposits

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

Other on-balance sheet financial instruments

The fair values of all other 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 reporting date for agreements of similar credit standing and maturity.

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

Valuation of financial instruments:

The Bank measures fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

Level 1: quoted prices in active markets for the same instrument (i.e., without modification or repacking);

Level 2: quoted prices in active markets for similar assets and liabilities or other valuation techniques for which all significant inputs are based on observable market data; and

Level 3: valuation techniques with significant inputs that are not based on observable market data.

B23 Fair value of financial instruments (continued)

The table below analyses financial instruments measured at fair value at the end of the reporting year:

31 December 2018	**Investment securities RO'000**	**Positive fair value of derivatives RO'000**	**Negative fair value of derivatives RO'000**	**Total RO'000**
Level 1	**7,360**	**-**	**-**	**7,360**
Level 2	**381,758**	**1,883**	**(3,702)**	**379,939**
Level 3	**2,500**	**-**	**-**	**2,500**
	391,618	**1,883**	**(3,702)**	**389,799**

31 December 2017 (Audited)	Investments RO'000	Positive fair value of derivatives RO'000	Negative fair value of derivatives RO'000	Total RO'000
Level 1	6,097	-	-	6,097
Level 2	315,704	1,744	(898)	316,550
Level 3	2,254	-	-	2,254
	324,055	1,744	(898)	324,901

Level 3 investments are investments in shares of an unquoted company, the shares of which are thinly traded. The management values the investment using net asset value of the investee based on the investee's financial statements, plus an applicable premium. Management considers the carrying value of the investment to approximate its fair value as a significant portfolio of the underlying investments of the investee company (a major turnkey project) is currently in the construction phase. Therefore, the carrying value is representative of fair value of the investments.

31 December 2018	**Investment securities USD'000**	**Positive fair value of derivatives USD'000**	**Negative fair value of derivatives USD'000**	**Total USD'000**
Level 1	**19,117**	**-**	**-**	**19,117**
Level 2	**991,579**	**4,891**	**(9,616)**	**986,854**
Level 3	**6,494**	**-**	**-**	**6,494**
	1,017,190	**4,891**	**(9,616)**	**1,012,465**

31 December 2017	Investments USD'000	Positive fair value of derivatives USD'000	Negative fair value of derivatives USD'000	Total USD'000
Level 1	15,836	-	-	15,836
Level 2	820,010	4,530	(2,332)	822,208
Level 3	5,854	-	-	5,854
	841,700	4,530	(2,332)	843,898

B24 Derivatives

In the ordinary course of business the Bank enters into various types of transactions that involve derivative financial instruments. A derivative financial instrument is a financial contract between two parties where payments are dependent upon movements in price in one or more underlying financial instruments, reference rate or index. These derivatives are stated at fair value. The fair value of a derivative is the equivalent of the unrealised gain or loss from marking to market the derivative using prevailing market rates or internal pricing models. Unrealised gains or losses are included in the statement of comprehensive income. The derivative financial instruments used by the Bank are described below:

B24.1 Derivative product types

Forwards and futures are contractual agreements to either buy or sell a specified currency, commodity or financial instrument at a specific price and date in the future.

Swaps are contractual agreements between two parties to exchange interest or foreign currency differentials based on a specific notional amount. For interest rate swaps, counter parties generally exchange fixed and floating rate interest payments based on a notional value in a single currency.

Options are contractual agreements that convey the right, but not the obligation, to either buy or sell a specific amount of a commodity, foreign currency or financial instrument at a fixed price, either at a fixed future date or at any time within a specified period.

B24.2 Derivatives held or issued for hedging purposes

As part of its asset and liability management the Bank uses derivatives for hedging purposes in order to reduce its exposure to currency and interest rate risks. This is achieved by hedging specific financial instruments and forecasted transactions as well as strategic hedging against overall statement of financial position exposures.

The Bank uses forward foreign exchange contracts, to hedge against specifically identified currency risks and to meet the net open position limit as specified by CBO.

Strategic hedging is carried out for interest rate risk by monitoring the re-pricing of financial assets and liabilities and entering into interest rate swaps to hedge a proportion of the interest rate exposure. As strategic hedging does not qualify for special hedge accounting, the related derivatives are accounted for as trading instruments.

The table below sets out the positive and negative fair values of derivative financial instruments, together with their notional amounts, analysed by term to maturity. The notional amounts, which provide an indication of the volumes of the transactions outstanding at the end of the period, do not necessarily reflect the amounts of future cash flows involved. These notional amounts, therefore, are neither indicative of the Bank's exposure to credit risk, which is generally limited to the positive fair value of the derivatives, nor to market risk.

B24 Derivatives (continued)

As at 31 December 2018	**Positive Fair Value**	**Negative Fair Value**	**Notional amount**	**Notional amounts by term to maturity**		
				Within 3 months	**3 - 12 months**	**More than 1 year**
	RO'000	**RO'000**	**RO'000**	**RO'000**	**RO'000**	**RO'000**
Forward foreign exchange purchase contracts	**51**	**3,660**	**440,506**	**276,027**	**164,479**	**-**
Interest rate swaps	**-**	**-**	**-**	**-**	**-**	**-**
Options	**-**	**-**	**-**	**-**	**-**	**-**
Forward foreign exchange sales contracts	**1,832**	**42**	**439,918**	**275,701**	**164,217**	**-**
Interest rate swaps	**-**	**-**	**-**	**-**	**-**	**-**
Options	**-**	**-**	**-**	**-**	**-**	**-**

As at 31 December 2017	Positive Fair Value	Negative Fair Value	Notional amount	Notional amounts by term to maturity		
				Within 3 months	3 - 12 months	More than 1 year
	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
Forward foreign exchange purchase contracts	431	164	709,094	446,350	252,844	9,900
Interest rate swaps	-	-	5,775	5,775	-	-
Options	246	246	44,352	-	44,352	-
Forward foreign exchange sales contracts	1,067	488	707,663	445,539	252,498	9,625
Interest rate swaps	-	-	5,775	5,775	-	-
Options	246	246	44,352	-	44,352	-

As at 31 December 2018	**Positive Fair Value**	**Negative Fair Value**	**Notional amount**	**Notional amounts by term to maturity**		
				Within 3 months	**3 - 12 months**	**More than 1 year**
	USD'000	**USD'000**	**USD'000**	**USD'000**	**USD'000**	**USD'000**
Forward foreign exchange purchase contracts	**133**	**9,507**	**1,144,171**	**716,953**	**427,218**	**-**
Interest rate swaps	**-**	**-**	**-**	**-**	**-**	**-**
Options	**-**	**-**	**-**	**-**	**-**	**-**
Forward foreign exchange sales contracts	**4,758**	**109**	**1,142,644**	**716,106**	**426,538**	**-**
Interest rate swaps	**-**	**-**	**-**	**-**	**-**	**-**
Options	**-**	**-**	**-**	**-**	**-**	**-**

As at 31 December 2017	Positive Fair Value	Negative Fair Value	Notional amount	Notional amounts by term to maturity		
				Within 3 months	3 - 12 months	More than 1 year
	USD'000	USD'000	USD'000	USD'000	USD'000	USD'000
Forward foreign exchange purchase contracts	1,119	425	1,841,803	1,159,351	656,739	25,714
Interest rate swaps	-	-	15,000	15,000	-	-
Options	639	639	115,200	-	115,200	-
Forward foreign exchange sales contracts	2,772	1,268	1,838,085	1,157,245	655,840	25,000
Interest rate swaps	-	-	15,000	15,000	-	-
Options	639	639	115,200	-	115,200	-

C1 Interest income

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
		Interest income on :		
257,218	**293,792**	Loans and advances to customers	**113,110**	99,029
7,039	**9,454**	Due from banks and other money market placements	**3,640**	2,710
19,574	**35,255**	Investments	**13,573**	7,536
283,831	**338,501**		**130,323**	109,275

C2 Interest expense

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
		Interest expense on :		
102,769	**109,631**	Customers' deposits	**42,208**	39,566
11,608	**6,364**	Subordinated loans	**2,450**	4,469
45,135	**75,273**	Due to banks and other money market borrowings	**28,980**	17,377
369	**88**	Compulsorily convertible bonds	**34**	142
159,881	**191,356**		**73,672**	61,554

C3 Net income earned from Islamic financing and investing activities

C3.a Gross income earned from Islamic financing and investing activities

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
16,992	**21,914**	Financing to customers	**8,437**	6,542
179	**532**	Due from banks and other money market placements	**205**	69
1,592	**2,416**	Investments	**930**	613
18,763	**24,862**		**9,572**	7,224

C3.b Profit paid to depositors / money market borrowings

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
8,470	**11,979**	Profit paid to depositors	**4,612**	3261
493	**784**	Profit paid to banks and other money market borrowings	**302**	190
8,963	**12,763**		**4,914**	3451
9,800	**12,099**	**Net income from Islamic financing and investing activities**	**4,658**	3773

C4 Other operating income

31 December 2017 USD'000	31 December 2018 USD'000		31 December 2018 RO'000	31 December 2017 RO'000
47,286	**40,804**	Fees and commission	**15,710**	18,205
14,350	**47,961**	Net gains from foreign exchange dealings	**18,465**	5,525
-	**(18)**	Loss on sale of fixed assets	**(7)**	-
309	**431**	Bad debt recovery	**166**	119
1,829	**3,075**	Dividend income	**1,184**	704
-	**(6,204)**	Losses from FVTPL investments	**(2,389)**	-
138	**-**	Gains on held for trading investments	**-**	53
63,912	**86,049**		**33,129**	24,606

C5 Other operating expenses

31 December 2017 USD'000	31 December 2018 USD'000		31 December 2018 RO'000	31 December 2017 RO'000
22,774	**25,442**	Operating and administration costs	**9,795**	8,768
-	**2,857**	Capital work in progress written off (B5)	**1,100**	-
6,642	**6,875**	Occupancy cost	**2,647**	2,557
338	**338**	Directors remuneration	**130**	130
179	**140**	Directors sitting fees	**54**	69
114	**130**	Shari'a supervisory board remuneration and sitting fees	**50**	44
30,047	**35,782**		**13,776**	11,568

C6 Loan impairment charges and other credit risk provisions, net

31 December 2017 USD'000	31 December 2018 USD'000		31 December 2018 RO'000	31 December 2017 RO'000
		Provided during the year:		
		Impairment charges provided/(released) on:		
18,223	**45,338**	Loans, advance and financing (B3)	**17,455**	7,016
-	**5,504**	Loan commitments and financial guarantees (B10)	**2,119**	-
2,509	**228**	Due from banks and other money market placements	**88**	966
-	**1,725**	Debt securities at amortised cost	**664**	-
-	**16**	Debt securities at FVOCI	**6**	-
-	**(543)**	Loans written back during the year	**(209)**	-
20,732	**52,268**	**Loan impairment charges and other credit risk provisions under IFRS 9, net**	**20,123**	7,982
		Portfolio impairment (under IAS 39) on:		
4,727	**-**	Loans, advances and financing	**-**	1,820
(195)	**-**	Lending to banks	**-**	(75)
25,264	**52,268**	Total portfolio impairment	**20,123**	9,727

C7 Income tax

a) Recognised in the statement of comprehensive income

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
		Tax expenses		
10,753	**12,878**	- Current tax	**4,958**	4,140
1,086	**275**	- Deferred tax expense	**106**	418
119	**-**	- Tax paid for prior year assessments	**-**	46
11,958	**13,153**	Income tax expenses recognised in statement of profit or loss	**5,064**	4,604
94	**242**	Recognised in other comprehensive income	**93**	36
12,052	**13,395**	**Total income tax expenses**	**5,157**	4,640

The Bank is liable for income tax for the year in accordance with the income tax laws of the Sultanate of Oman at the rate of 15% on its taxable profits.

b) Reconciliation

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
77,754	**89,428**	Profit before tax for the year	**34,430**	29,935
11,663	**13,416**	Income tax as per rate mentioned above	**5,165**	4,490
		Tax impact of:		
1,407	**1,031**	- non-deductible expenses/losses	**397**	542
(1,205)	**(1,294)**	- tax exempt income	**(498)**	(464)
(26)	**-**	- increase in tax rate	**-**	(10)
119	**-**	- Tax paid for prior year assessments	**-**	46
11,958	**13,153**	Income tax expense	**5,064**	4,604

c) Deferred tax (liability) / asset

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
(982)	**(299)**	On profit or loss items	**(115)**	(378)
244	**(956)**	On other comprehensive income items	**(368)**	94
(738)	**(1,255)**		**(483)**	(284)

d) Tax assessment

Tax assessments of the Bank for the years 2007 to 2015 have been completed and for the year 2016 and 2017 have not yet been agreed with the Secretariat General for Taxation at the Ministry of Finance. The Bank is of the opinion that additional taxes, if any, related to the open tax years would not be significant to the financial position of the Bank as at 31 December 2018.

C7 Income tax (continued)

e) Movement of current tax provision

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
8,361	**10,771**	Balance as at the beginning of the year	**4,147**	3,219
10,753	**12,878**	Charge during the year	**4,958**	4,140
(8,343)	**(10,693)**	Paid during the year	**(4,117)**	(3,212)
10,771	**12,956**	Balance as at the end of the year	**4,988**	4,147

f) Movement of deferred tax asset/(liability)

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
442	**(738)**	Balance as at the beginning of the year	**(284)**	170
561	**2,093**	Charge during the year	**806**	216
(1,741)	**(2,610)**	Created during the year	**(1,005)**	(670)
(738)	**(1,255)**	Balance as at the end of the year	**(483)**	(284)

C8 Basic and diluted earnings per share

Basic earnings per share are calculated by dividing net profit for the year by the weighted average number of shares outstanding during the year.

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
65,796	**76,275**	Profit for the year	**29,366**	25,331
-	**(20,130)**	Less: Additional Tier 1 Coupon	**(7,750)**	-
-	**(145)**	Less: issue expenses – Additional Tier 1 capital	**(56)**	-
65,796	**56,000**	Profit for the year attributable to equity holders of the Bank after coupon and issuance cost on Additional Tier 1 capital securities	**21,650**	25,331
1,982,646	**1,982,646**	Weighted average number of shares outstanding during the year (in thousands)	**1,982,646**	1,982,646
3.32	**2.83**	Basic earnings per share for the year (**cents / baizas**)	**10.918**	12.776

In the Annual General Meeting held on 29 March 2018, the shareholders approved the Board's recommendation to distribute 10% bonus shares resulting in the issuance of 178,464,624 new shares.

C8 Basic and diluted earnings per share (continued)

Diluted earnings per share is calculated by dividing the net profit attributable to ordinary shareholders (after adjusting for interest on the compulsorily convertible bonds, net of income tax) for the year by the weighted average number of ordinary shares including the dilutive potential of ordinary shares that would be issued on the conversion of the compulsorily convertible bonds into ordinary shares. The compulsorily convertible bonds was fully converted as of 31 December 2018.

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
65,796	**56,000**	Profit for the year attributable to equity holders of the Bank after coupon and issuance cost on Additional Tier 1 capital securities	**21,650**	25,331
312	**-**	Interest on convertible bonds, net of income tax	**-**	120
66,108	**56,000**		**21,650**	25,451
2,001,562	**1,982,646**	Weighted average number of shares outstanding after dilution during the year (in thousands)	**1,982,646**	2,001,562
3.30	**2.83**	Diluted earnings per share for the year (**cents / baizas**)	**10.918**	12.716

The reconciliation of weighted average number of shares shown under basic earnings and diluted earnings are as follow:

	31 December 2018 In thousands	31 December 2017 In thousands
Weighted average number of shares outstanding during the year	**1,982,646**	1,982,646
Dilutive potential of ordinary shares to be issued on the conversion of convertible bonds	**-**	18,916
Weighted average number of shares outstanding during the year	**1,982,646**	2,001,562

D Financial risk management

The primary objective of the risk management is to safeguard the Bank's capital and its financial resources from various risks. The Bank has exposure to the following risks from its use of financial instruments:

- Credit risk
- Liquidity risk
- Market risk
- Operational risk

The Board of Directors has overall responsibility for the establishment and oversight of the Bank's risk management framework. Such responsibility is discharged by the Board through a Board Risk Committee (BRC), constituted by the Board which is responsible for developing and monitoring the Bank's risk management policies. BRC submits periodic reports to the Board, appraising it on various aspects of risk and changes in the risk profile of the Bank.

The risk management policies focus on identification, measurement, monitoring and mitigation of risk, irrespective of its manner of manifestation. In this process, the Bank recognises that the dynamics of markets may necessitate decisions that may deviate on occasions from the principles of CRM. For such requirements, minimal and requisite level of flexibilities is to build into the Risk Management policies, along with suitable and adequate safeguards/controls.

The Bank's Audit Committee is responsible for monitoring compliance with the Bank's risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Bank. The Audit Committee is assisted in these functions by Internal Audit department. Internal Audit department undertakes both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported to the Audit Committee.

D Financial risk management (continued)

There are sub-committees at management level for managing risks. The Asset and Liability Committee (ALCO) manages the risks in the balance sheet arising out of liquidity management, interest rates management as well as tenor of exposures taken by the Bank. ALCO provides management with guidance on managing these risks. Risk appetite is articulated through various limits, ratios and caps. Operational Risk is managed under the guidance of Operational Risk Committee (ORCO) at the management level. A separate ALCO has also been established to monitor the performance of the assets of Sohar Islamic. Bank has established a Management Risk Committee (MRC) to oversee the risk management function and to establish an improved and enhanced risk awareness and risk culture with the bank.

D1 Credit risk

Credit risk is the risk of financial loss to the Bank if counterparty to a financial instrument fails to meet its contractual obligations, in simpler terms; it represents the probability of default by any counterparty in repayment of principal obligations and / or servicing interest obligations in accordance with the set redemption schedule or terms of contract.

D1.1 Management of credit risk

The Board of Directors has delegated responsibility for the monitoring of credit risk to its Board Risk Committee and is responsible for handling all facets of risk for both Islamic and conventional banking division. The Bank has a Chief Risk Officer who heads the management of Risk reporting to the Board Risk Committee. Credit risk is managed by the following:

- setting up risk limits and boundaries, within the regulatory guidelines, for risk origination to be within the approved risk appetite of the Bank;
- Credit risk at the origination is managed and controlled through a time tested credit appraisal process which includes independent credit risk review of individual corporate credit proposals and through a Board approved retail products policy and template lending. Exceptions are reviewed by Credit Risk function.
- continuous monitoring of these stand-alone credit risks in the ‘corporate’ and ‘emerging corporate’ portfolio as well as in the retail credit portfolio through an independent loan review group (LRG), reporting to Board Risk Committee of the Board, for risk grading of the portfolios and tracking the movement of the grades;
- portfolio credit risk measurement through tracking on the set portfolio risk parameters such as concentration risk; Approved credit transactions are periodically reviewed in Loan Review process on sample basis, to check appropriate policy/standard. The process also helps conducting gap analysis in credit assessment process.
- the Bank will not entertain credit proposals from entities/individuals whose name appears in the CBO classified list under Bank Credit and Statistical Bureau (BCSB). However, in exceptional cases in the retail business unit, loans are approved with strong justifications and risk mitigations for considering any such proposals, which in turn have to be referred to delegated authorities as per the retail loan policy;
- limiting concentrations of exposure to counterparties, geographic locations and industries (for loans and advances), and by issuer, market liquidity and country (for investment securities);
- developing and maintaining the Bank’s risk grading in order to categorise exposures according to the degree of risk of financial loss faced and to focus management’s attention on the attendant risks; and
- providing advice, guidance and specialist skills to business units to promote best practice throughout the Bank in the management of credit risk.

The Bank employs a range of policies and practices to mitigate credit risk. The Bank follows a risk mitigation practice of identifying business cash flows as the primary driver for the advances extended. These cash flows are then tested for sustainability over the tenor of the credit facility and a suitable mechanism is put in place to capture the same into the client account with the Bank. To cover unforeseen risk, which dries up the cash flows, additional tangible securities are taken such as real estate or equity shares. The Bank implements guidelines on the acceptability of specific classes of collateral credit risk mitigation. The principal types of collaterals for loans and advances are:

- mortgages over properties;
- charges of assets under murabaha agreements;
- ownership/title of assets under Ijarah financing ;
- charges over business assets such as premises inventory and accounts receivable; and
- Charges over financial instruments such as debt securities and equities.

All loans and advances of the Bank are regularly monitored to ensure compliance with the stipulated repayment terms. Those loans and advances are classified into one of the 5 risk classification categories: Standard, Special Mention, Substandard, Doubtful and Loss – as required by CBO regulations and guidelines. Further, as mandated by IFRS 9, the loans and advances are also classified into stage 1, stage 2 and stage 3 based on the internal credit ratings / significant increase in credit risk criteria / requirements of CBO circular BM 1149. The responsibility for identifying problem accounts and classifying them rests with business line function and a separate unit has been set up to manage problem accounts.

D Financial risk management (continued)

D1 Credit risk (continued)

D1.2 Exposure to credit risk

The following table sets out information about the credit quality of financial assets measured at amortised cost. Unless specifically indicated, for financial assets, the amounts in the table represent gross carrying amounts.

31 December 2018	12-Month ECL RO'000	Lifetime ECL not credit - impaired RO'000	Lifetime ECL credit - impaired RO'000	Total RO'000
Loans and advances to customers - corporate banking				
Performing loans (Grades 1-5)	847,899	182,789	671	1,031,359
Performing loans (Grades 6)	256,125	45,012	18	301,155
Performing loans (Grades 7)	16	186,618	12	186,646
Non-performing loans (Grades 8-10)	701	276	58,086	59,063
Gross loans and advances to customers - corporate banking	1,104,741	414,695	58,787	1,578,223
Loans and advances to customers – retail banking				
Performing loans (Grades 1-7)	721,007	23,231	-	744,238
Non-performing loans (Grades 8-10)	-	-	18,199	18,199
Gross loans and advances to customers - retail banking	721,007	23,231	18,199	762,437
Total gross loans and advances to customers	1,825,748	437,926	76,986	2,340,660
Credit related contingent items				
Performing loans (Grades 1-5)	250,570	-	-	250,570
Performing loans (Grades 6)	375,855	-	-	375,855
Performing loans (Grades 7)	-	104,844	-	104,844
Non-performing loans (Grades 8-10)	-	-	1,646	1,646
Total gross contingent items to customers	626,425	104,844	1,646	732,915
Due from banks and money market placements	113,179	8,666	-	121,845
Investment securities	350,388	51,040	-	401,428

D Financial risk management (continued)

D1 Credit risk (continued)

D1.2 Exposure to credit risk (continued)

31 December 2018	12-Month ECL USD'000	Lifetime ECL not credit - impaired USD'000	Lifetime ECL credit - impaired USD'000	Total USD'000
Loans and advances to customers - corporate banking				
Performing loans (Grades 1-5)	2,202,335	474,777	1,743	2,678,855
Performing loans (Grades 6)	665,260	116,914	47	782,221
Performing loans (Grades 7)	42	484,722	31	484,795
Non-performing loans (Grades 8-10)	1,821	717	150,873	153,411
Gross loans and advances to customers - corporate banking	2,869,458	1,077,130	152,694	4,099,281
Loans and advances to customers – retail banking				
Performing loans (Grades 1-7)	1,872,745	60,340	-	1,933,085
Non-performing loans (Grades 8-10)	-	-	47,270	47,270
Gross loans and advances to customers - retail banking	1,872,745	60,340	47,270	1,980,355
Total gross loans and advances to customers	4,742,203	1,137,470	199,964	6,079,636
Credit related contingent items				
Performing loans (Grades 1-5)	650,831	-	-	650,831
Performing loans (Grades 6)	976,247	-	-	976,247
Performing loans (Grades 7)	-	272,322	-	272,322
Non-performing loans (Grades 8-10)	-	-	4,275	4,275
Total gross contingent items to customers	1,627,078	272,322	4,275	1,903,675
Due from banks and money market placements	293,971	22,509	-	316,480
Investment securities	910,099	132,571	-	1,042,670

D Financial risk management (continued)

Subject to CBO approval

D1 Credit risk (continued)

D1.2 Exposure to credit risk (continued)

1 January 2018	12-Month ECL RO'000	Lifetime ECL not credit - impaired RO'000	Lifetime ECL credit - impaired RO'000	Total RO'000
Loans and advances to customers - corporate banking				
Performing loans (Grades 1-5)	968,651	193,884	4,455	1,166,990
Performing loans (Grades 6)	201,090	23,412	-	224,502
Performing loans (Grades 7)	-	50,909	541	51,450
Non-performing loans (Grades 8-10)	-	-	38,149	38,149
Gross loans and advances to customers - corporate banking	1,169,741	268,205	43,145	1,481,091
Loans and advances to customers – retail banking				
Performing loans (Grades 1-7)	637,349	18,167	-	655,516
Non-performing loans (Grades 8-10)	-	-	11,624	11,624
Gross loans and advances to customers - retail banking	637,349	18,167	11,624	667,140
Total gross loans and advances to customers	1,788,383	305,080	54,768	2,148,231
Credit related contingent items				
Performing loans (Grades 1-5)	426,651	-	-	426,651
Performing loans (Grades 6)	182,850	17,478	-	200,328
Performing loans (Grades 7)	-	157,306	-	157,306
Non-performing loans (Grades 8-10)	-	-	1,944	1,944
Total gross contingent items to customers	609,501	174,784	1,944	786,229
Due from banks and money market placements	97,542	-	7,700	105,242
Investment securities	91,750	-	-	91,750

D Financial risk management (continued)

D1 Credit risk (continued)

D1.2 Exposure to credit risk (continued)

Subject to CBO approval

1 January 2018	12-Month ECL USD'000	Lifetime ECL not credit - impaired USD'000	Lifetime ECL credit - impaired USD'000	Total USD'000
Loans and advances to customers - corporate banking				
Performing loans (Grades 1-5)	2,515,978	503,595	11,571	3,031,144
Performing loans (Grades 6)	522,312	60,810	-	583,122
Performing loans (Grades 7)	-	132,231	1,405	133,636
Non-performing loans (Grades 8-10)	-	-	99,088	99,088
Gross loans and advances to customers - corporate banking	3,038,290	696,636	112,064	3,846,990
Loans and advances to customers – retail banking				
Performing loans (Grades 1-7)	1,655,452	47,187	-	1,702,639
Non-performing loans (Grades 8-10)	-	-	30,192	30,192
Gross loans and advances to customers - retail banking	1,655,452	47,187	30,192	1,732,831
Total gross loans and advances to customers	4,693,742	743,823	142,256	5,579,821
Credit related contingent items				
Performing loans (Grades 1-5)	1,108,184	-	-	1,108,184
Performing loans (Grades 6)	474,935	45,397	-	520,332
Performing loans (Grades 7)	-	408,587	-	408,587
Non-performing loans (Grades 8-10)	-	-	5,049	5,049
Total gross contingent items to customers	1,583,119	453,984	5,049	2,042,152
Due from banks and money market placements	253,356	-	20,000	273,356
Investment securities	238,312	-	-	238,312

Maximum exposure to credit risk before collateral held or other credit enhancements for all on-balance sheet assets are based on net carrying amounts as reported in the statement of financial position.

The maximum credit risk exposures relating to off-balance sheet items calculated as per Basel II guidelines are provided in note D5. The amounts represented in note D5 represent a worst case scenario of credit risk exposure as of 31 December 2018 and 2017, without taking into account of any collateral held or other credit enhancements attached.

D Financial risk management (continued)

D1 Credit risk (continued)

D1.2 Exposure to credit risk (continued)

Impairment assessment ***(Policy applicable from 1 January 2018)***

Definition of default and cure
The Bank considers a financial instrument defaulted and therefore Stage 3 (credit-impaired) for ECL calculations in all cases when the borrower becomes 90 days past due on its contractual payments. The Bank considers treasury and interbank balances defaulted and takes immediate action when the required intraday payments are not settled by the close of business as outlined in the individual agreements.

As a part of a qualitative assessment of whether a customer is in default, the Bank also considers a variety of instances that may indicate unlikeliness to pay. When such events occur, the Bank carefully considers whether the event should result in treating the customer as defaulted and therefore assessed as Stage 3 for ECL calculations or whether Stage 2 is appropriate. Such events include:

- Internal rating of the borrower indicating default or near-default and/or substantial downgrade of rating
- The borrower requesting emergency funding from the Bank
- The borrower having past due liabilities to public creditors or employees
- The borrower is deceased
- A material decrease in the underlying collateral value where the recovery of the loan is expected from the sale of the collateral
- A material decrease in the borrower's turnover or the loss of a major customer and material decrease of profit
- A covenant breach not waived by the Bank
- Unexplained delay in commercial operation
- Unreliable or delay in submission of financial statements The debtor (or any legal entity within the debtor's group) filing for bankruptcy application/protection • Debtor's listed debt or equity suspended at the primary exchange because of rumours or facts about financial difficulties

It is the Bank's policy to consider a financial instrument as 'cured' and therefore re-classified out of Stage 3 when none of the default criteria have been present for at least twelve consecutive months which is six months for accounts classified as Stage 2. The decision whether to classify an asset as Stage 2 or Stage 1 once cured depends on the updated credit grade, at the time of the cure, and whether this indicates there has been a significant increase in credit risk compared to initial recognition.

Incorporation of forward-looking information
The Bank incorporates forward-looking information into both its assessment of whether the credit risk of an instrument has increased significantly since its initial recognition and its measurement of ECL. Based on consideration of a variety of external actual and forecast information, the bank formulates a fundamental view of the future direction of relevant economic variables as well as a reasonable range of possible scenarios.

Given the nature of the bank's exposures and availability of historical statistically reliable information, the bank derives the point-in-time (PIT) probability of default (PD) using the through-the-cycle (TTC) PD data computed from historical bank default data for each rating category. TTC PDs are determined by utilizing macroeconomic variables and non-cyclical risk drivers to predict default rates over an economic cycle. The bank uses the flow rate analysis model to link the TTC PDs with forward looking economic factors to drive PIT PD estimates for each Moody's rating category. The macroeconomic model takes into consideration forward looking economic forecasts under three scenarios (base case, economic downturn as negative case and economic upturn as positive case), historical economic data, the asset correlation of each rating category, and TTC PDs for deriving PIT PDs. The relationship between the economic factors and default and loss rates have been developed using internal historical data and relevant external market data.

The Bank's internal rating and PD estimation process
The Bank's independent Credit Risk Department operates its internal rating models. The Bank runs separate models for its key portfolios in which its customers are rate from 1 to 10 using internal grades. The models incorporate both qualitative and quantitative information and, in addition to information specific to the borrower, utilise supplemental external information that could affect the borrower's behaviour. Where practical, they also build on information from Good Rating Agency. These information sources are first used to determine the PDs within the Bank's Basel III framework. The internal credit grades are assigned based on these Based III grades.

PDs are then adjusted for IFRS 9 ECL calculations to incorporate forward looking information and the IFRS 9 Stage classification of the exposure. This is repeated for each economic scenarios as appropriate.

D Financial risk management (continued)

D1 Credit risk (continued)

D1.2 Exposure to credit risk (continued)

Impairment assessment *(Policy applicable from 1 January 2018) (continued)*

Generating the term structure of Probability of Default (PD)
The bank employs statistical models to analyse the data collected and generate estimates of PD of exposures and how these are expected to change as a result of the passage of time. This analysis includes the identification and calibration of relationships between changes in default rates and changes in key macro-economic factors, across various geographies in which the bank has exposures.

The Bank's internal credit rating grades along with the respective PDs are as below:

Internal rating grades	Internal rating grade description	PD range (%)
1	Investment grade	0.10% to 2.00%
2	Investment grade	
3	Investment grade	
4	Investment grade	
5	Investment grade	
6	Investment grade	
7	Sub-investment grade	3.70%
8 - 10	Non-performing	6.60% to 20.00%

Economic variable assumptions
The Bank obtains the data used from third party sources (World Bank and other public and private sources) to verify the accuracy of inputs to the Bank's ECL models including determining the weights attributable to the multiple scenarios. For the implemented ECL model for corporate and SME segment, a principal component analysis was done to form composite index (CI) consisting of following three variable namely
(1) GDP per Capita, Constant Prices (National Currency, change, no lag)
(2) Volume of Import of Goods (% Change, lag 1) and
(3) General Government Revenue (% of GDP, lag 3).

Projected composite index (CI) for next four years are as following.

Period	CI_Baseline	CI_Downturn	CI_Upturn
2019	0.93	0.55	1.32
2020	0.43	0.05	0.82
2021	0.10	-0.29	0.49
2022	-0.14	0.53	0.24

These economic variables and their associated impact on the PD, EAD and LGD vary by financial instrument. Expert judgment has also been applied in this process. Forecasts of these economic variables (the "base economic scenario") are are collected from statistical database of World Bank and other public and private sources to provide the best estimate view of the economy over the next five years. After five years, to project the economic variables out for the full remaining lifetime of each instrument, a mean reversion approach has been used, which means that economic variables tend to either a long run average rate (e.g. for unemployment) or a long run average growth rate (e.g. GDP) over a period of two to five years. The impact of these economic variables on the PD, EAD and LGD has been determined by performing statistical regression analysis to understand the impact changes in these variables have had historically on default rates and on the components of LGD and EAD.

D Financial risk management (continued)

D1 Credit risk (continued)

D1.2 Exposure to credit risk (continued)

Impairment assessment ***(Policy applicable from 1 January 2018) (continued)***

Economic variable assumptions (continued)
As with any economic forecasts, the projections and likelihoods of occurrence are subject to a high degree of inherent uncertainty and therefore the actual outcomes may be significantly different to those projected. The bank considers these forecasts to represent its best estimate of the possible outcomes and has analysed the non-linearities and asymmetries within the bank's different portfolios to establish that the chosen scenarios are appropriately representative of the range of possible scenarios.

Other forward-looking considerations not otherwise incorporated within the above scenarios, such as the impact of any regulatory, legislative or political changes, have also been considered, but are not deemed to have a material impact and therefore no adjustment has been made to the ECL for such factors. This is reviewed and monitored for appropriateness on a quarterly basis.

Treasury, trading and interbank relationships
The Bank's treasury, trading and interbank relationships and counterparties comprise financial services institutions, banks, broker-dealers, exchanges and clearing-houses. For these relationships, the Bank's credit risk department analyses publicly available information such as financial information and other external data, e.g., the rating of Moody's or equivalent, and assigns the internal rating.

Corporate and small business lending
For corporate and investment banking loans, the borrowers are assessed by specialised credit risk employees of the Bank. The credit risk assessment is based on a credit scoring model that takes into account various historical, current and forward-looking information such as:

- Historical financial information together with forecasts and budgets prepared by the client. This financial information includes realised and expected results, solvency ratios, liquidity ratios and any other relevant ratios to measure the client's financial performance. Some of these indicators are captured in covenants with the clients and are, therefore, measured with greater attention.
- Any publicly available information on the clients from external parties. This includes external rating grades issued by rating agencies, independent analyst reports, publicly traded bond or CDS prices or press releases and articles.
- Any macro-economic or geopolitical information, e.g., GDP growth relevant for the specific industry and geographical segments where the client operates.
- Any other objectively supportable information on the quality and abilities of the client's management relevant for the company's performance.
- The complexity and granularity of the rating techniques varies based on the exposure of the Bank and the complexity and size of the customer. Some of the less complex small business loans are rated within the Bank's models for retail products.

Consumer lending and retail mortgages
Consumer lending comprises unsecured personal loans, credit cards and overdrafts. These products along with retail mortgages and some of the less complex small business lending are rated by an automated scorecard tool primarily driven by days past due. Other key inputs into the models are:
- Consumer lending products: use of limits and volatility thereof, GDP growth, unemployment rates, changes in personal income/salary levels based on records of current accounts, personal indebtedness and expected interest repricing
- Retail mortgages: GDP growth, unemployment rates, changes in personal income/salary levels based on records of current accounts, personal indebtedness and expected interest repricing

Exposure at default

The exposure at default (EAD) represents the gross carrying amount of the financial instruments subject to the impairment calculation, addressing both the client's ability to increase its exposure while approaching default and potential early repayments too.

To calculate the EAD for a Stage 1 loan, the Bank assesses the possible default events within 12 months for the calculation of the 12mECL. However, if a Stage 1 loan that is expected to default in the 12 months from the balance sheet date and is also expected to cure and subsequently default again, then all linked default events are taken into account. For Stage 2, Stage 3 and POCI financial assets, the exposure at default is considered for events over the lifetime of the instruments.

The Bank determines EADs by modelling the range of possible exposure outcomes at various points in time, corresponding the multiple scenarios. The IFRS 9 PDs are then assigned to each economic scenario based on the outcome of Bank's models.

D Financial risk management (continued)

D1 Credit risk (continued)

D1.2 Exposure to credit risk (continued)

Impairment assessment *(Policy applicable from 1 January 2018) (continued)*

Loss given default
For corporate and investment banking financial instruments, LGD values are assessed at least every twelve months by account managers and reviewed and approved by the Bank's specialised credit risk department. The credit risk assessment is based on a standardised LGD assessment framework that results in a certain LGD rate. These LGD rates take into account the expected EAD in comparison to the amount expected to be recovered or realised from any collateral held.

The Bank segments its retail lending products into smaller homogeneous portfolios, based on key characteristics that are relevant to the estimation of future cash flows. The applied data is based on historically collected loss data and involves a wider set of transaction characteristics (e.g., product type, wider range of collateral types) as well as borrower characteristics.

Further recent data and forward-looking economic scenarios are used in order to determine the IFRS 9 LGD rate for each group of financial instruments. When assessing forward-looking information, the expectation is based on multiple scenarios. Examples of key inputs involve changes in, collateral values including property prices for mortgages, commodity prices, payment status or other factors that are indicative of losses in the bank.

The Bank estimates regulatory and IFRS 9 LGDs on a different basis. Under IFRS 9, LGD rates are estimated for the Stage 1, Stage 2, Stage 3 and POCI IFRS 9 segment of each asset class. The inputs for these LGD rates are estimated and, where possible, calibrated through back testing against recent recoveries. These are repeated for each economic scenario as appropriate.

Significant Increase in Credit Risk
The Bank continuously monitors all assets subject to ECLs. In order to determine whether an instrument or a portfolio of instruments is subject to 12mECL or LTECL, the Bank assesses whether there has been a significant increase in credit risk since initial recognition.

The Bank also applies a secondary qualitative method for triggering a significant increase in credit risk for an asset, such as moving a customer/facility to the watch list, or the account becoming forborne. In certain cases, the Bank may also consider that events set out below are a significant increase in credit risk as opposed to a default. Regardless of the change in credit grades, if contractual payments are more than 30 days past due, the credit risk is deemed to have increased significantly since initial recognition.

a. Inadequate or unreliable financial or other information such as unavailability of audited financial statements within 120 days from end of accounting period.
b. Delay in documentation execution over 35 days from limit set up due to disputes with customers.
c. Borrower is subject to litigation by third parties that may have a significant impact on his financial position.
d. Frequent changes in key senior management personnel without acceptable successors or professional management.
e. Intra Group transfer of funds without underlying transactions beyond 50% of Tangible Net Worth.
f. Deferment/delay in the date for commencement of commercial operations by more than one year except in Government projects or delays are due to Government approvals.
g. Modifications of terms resulting in concessions granted to the borrower (after examining the cash flows of the borrower/financial position/ability to repay) including extension of moratorium, deferment of payment, waiver of covenants etc. This requirement shall be in conformity to the restructuring guidelines issued by CBO from time to time.
h. A fall of 25% or more in the turnover or in the EBIT as compared to the previous year except in the case of change in business model/one of material events.
i. A fall in Debt Service coverage ratio to below 1 except in cases which have acceptable external credit support.
j. Rating downgrade by 3 notches for ratings from R1 to R4 and 2 notches downgrade for R5 and R6.
k. Erosion in net worth by more than 20% compared to previous year coupled with increase in leverage by 1.5 times.

Model risk management:
The Bank has utilised models in many of its financial and business activities from underwriting a credit facility to reporting expected loss under the IFRS9 accounting standards.

To manage the model risks, the bank has implemented the IFRS 9 Governance Framework (the Framework). The Framework is a bank wide policy and is applicable to all models of the bank. According to the Framework, all internally or externally (vendor based) developed risk quantification models that directly affect the financial reporting on Expected Loss (EL) and Lifetime Expected Loss (LEL) require independent validation.

The Framework establishes a systematic approach to manage the development, validation, approval, implementation and on-going use of the models. It sets out an effective management structure with clearly defined roles and responsibilities, policies and controls for managing model risk. The Framework is reviewed on a regular basis to ensure it meets regulatory standards and international practices. Any major change to the Framework must be approved by the Board of Directors or the BRC.

D1.3 Credit rating analysis

The table below presents an analysis of debt securities, treasury bills and other eligible bills by rating agency designation at 31 December 2018, based on Moody's ratings or equivalent.

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
10,320	**-**	Baa2	**-**	3,973
25,707	**6,514**	BBB	**2,508**	9,897
-	**41,413**	Baa3	**15,944**	-
43,449	**59,002**	Unrated bonds	**22,716**	16,728
965,862	**1,258,481**	Sovereign securities	**484,515**	371,857
1,045,338	**1,365,410**	**Total**	**525,683**	402,455

The following table shows the gross placements held with counterparties at the reporting date:

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
114,831	**103,701**	Aaa1 to Aaa3	**39,925**	44,210
31,631	**9,927**	A1 to A3	**3,822**	12,178
47,050	**180,262**	Baa1 to Baa3	**69,401**	18,114
19,075	**509**	Ba1 to Ba3	**196**	7,344
45,600	**22,081**	B1 to Caa	**8,501**	17,556
15,169	**-**	Unrated	**-**	5,840
273,356	**316,480**	**Total**	**121,845**	105,242

The Bank performs an independent assessment based on quantitative and qualitative factors in cases where a Bank is unrated.

D Financial risk management (continued)

D1 Credit risk (continued)

D1.4 Collateral securities

The Bank holds collateral against loans, advances and financing to customers in the form of mortgage interests over property, other registered securities, assets and guarantees. Estimates of fair value are based on the value of the collateral assessed at the time of borrowing and updated once in three years, except when a loan is individually assessed as impaired. In appropriate cases, two valuation reports are also collected for validation. The shares of MSM listed companies which are taken as securities are valued on a fortnightly basis, unless it is a highly volatile stock whereby the valuation is done on daily basis.

An estimate of the fair value of collateral and other security enhancements held against loans, advances and financing is shown below:

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
		Against past due but not impaired		
267,971	**686,556**	Property	**264,324**	103,169
2,943	**3,740**	Equity	**1,440**	1,133
61,465	**249,325**	Commercial mortgage	**95,990**	23,664
32,073	**9,693**	Vehicles	**3,732**	12,348
11,088	**24,564**	Fixed deposits	**9,457**	4,269
375,540	**973,878**	**Total**	**374,943**	144,583
		Against past due and impaired		
33,449	**59,475**	Property	**22,898**	12,878
-	**26,847**	Commercial mortgage	**10,336**	
1,571	**621**	Vehicles	**239**	605
35,020	**86,943**	**Total**	**33,473**	13,483
		Against neither past due nor impaired		
1,330,608	**1,735,195**	Property	**668,050**	512,284
578,597	**607,468**	Commercial mortgage	**233,875**	222,760
77,247	**157,912**	Fixed deposits	**60,796**	29,740
121,157	**54,086**	Equity	**20,823**	46,645
62,379	**46,618**	Vehicles	**17,948**	24,016
2,169,987	**2,601,279**	**Total**	**1,001,492**	835,445
2,580,548	**3,662,100**	**Total collateral held**	**1,409,908**	993,511

D1.5 Settlement risk

Settlement risk is the risk of loss due to the failure of a party to honour its obligations to deliver cash, securities or other assets as contractually agreed on the day of settlement.

In foreign exchange trades, though there is fulfilment of both the legs of the transaction on the settlement date as is common practice between trading partners (free settlement), there will be risk on account of different time zones. In these cases, the settlement risk is mitigated through the execution of bilateral payment netting agreements.

D1.6 Concentrations

Concentrations of credit risk arise when a number of counter parties are engaged in similar business activities or activities in the same geographic region or have similar economic features that would cause their ability to meet contractual obligations to be affected similarly by changes in economic, political or other conditions. Concentrations of credit risk indicate the relative sensitivity of the Bank's performance to developments affecting a particular industry or geographic location.

D Financial risk management (continued)

D1 Credit risk (continued)

D1.6 Concentrations (continued)

The Bank manages its credit risk exposure through diversification of lending activities to avoid undue concentrations of risks with individuals or group of customers in specific locations or businesses. It also obtains appropriate security. Concentration of the gross credit exposure is given below:

	31 December 2018			31 December 2017		
	Loans, advances and financing RO'000	**Due from banks and other money market placements RO'000**	**Debt securities RO'000**	Loans, advances and financing RO'000	Due from banks and other money market placements RO'000	Debt securities RO'000
Concentration by sector						
Corporate	**1,578,223**	**-**	**41,168**	1,481,091	-	29,885
Personal	**762,437**	**-**	**-**	667,140	-	-
Sovereign	**-**	**-**	**484,515**	-	-	372,570
Banks	**-**	**121,845**		-	105,242	-
	2,340,660	**121,845**	**525,683**	2,148,231	105,242	402,455
Concentration by location						
Middle east	**2,299,850**	**54,342**	**245,791**	2,143,610	47,372	214,251
Europe	**39,270**	**60,528**	**5,775**	-	27,093	3,154
North America	**-**	**5,057**	**274,117**	-	4,128	185,050
Asia	**1,540**	**1,918**	**-**	4,621	26,642	-
Australia	**-**	**-**	**-**	-	7	-
	2,340,660	**121,845**	**525,683**	2,148,231	105,242	402,455

	31 December 2018			31 December 2017		
	Loans, advances and financing USD'000	**Due from banks and other money market placements USD'000**	**Debt securities USD'000**	Loans, advances and financing USD'000	Due from banks and other money market placements USD'000	Debt securities USD'000
Concentration by sector						
Corporate	**4,099,281**	**-**	**106,929**	3,846,990	-	77,624
Personal	**1,980,355**	**-**	**-**	1,732,831	-	-
Sovereign	**-**	**-**	**1,258,481**	-	-	967,714
Banks	**-**	**316,480**	**-**	-	273,356	-
	6,079,636	**316,480**	**1,365,410**	5,579,821	273,356	1,045,338
Concentration by location						
Middle east	**5,973,636**	**141,147**	**638,418**	5,520,822	123,044	556,497
Europe	**102,000**	**157,216**	**15,000**	-	70,371	8,192
North America	**-**	**13,135**	**711,992**	-	10,722	480,649
Asia	**4,000**	**4,982**	**-**	12,003	69,200	-
Australia	**-**	**-**	**-**	-	18	-
	6,079,636	**316,480**	**1,365,410**	5,579,821	273,356	1,045,338

Refer to B3 for an analysis by economic sector

D Financial risk management (continued)

D1 Credit risk (continued)

D1.6 Concentrations (continued)

Concentration by location for loans and advances is measured based on the location of the entity holding the asset, which has a high correlation with the location of the borrower. Concentration by location for investment securities is measured based on the location of the issuer of the security. The Bank seeks to manage its credit risk exposure through diversification of lending activities to avoid undue concentrations of risk with banks or customers in a specific currency. It also obtains security when appropriate. An analysis of the Bank's gross exposure to relevant segments is provided in note E.

D2 Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting its obligations that are settled by delivering cash or another financial asset.

D2.1 Management of liquidity risk

The Bank's approach to managing liquidity is to ensure, as far as possible, that it always has sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions without incurring unacceptable losses or risking damage to the Bank's reputation. The Bank has put in place an approved Contingency Liquidity Plan to facilitate management of liquidity.

Liquidity risk is managed by the Bank through closely monitoring the liquidity gap against fixed limits.

Liquidity is provided by Treasury, which receives information from other business units regarding the liquidity profile of their financial assets and liabilities and details of other projected cash flows arising from projected future business. Treasury maintains a portfolio of short-term liquid assets, largely made up of short-term liquid investment securities, loans and advances to banks and other inter-bank facilities, to ensure that sufficient liquidity is maintained within the Bank. In this process due care is taken to ensure the Bank complies with all the Central Bank regulations.

The Bank conducts stress testing on liquidity based on assumptions approved by ALCO and CBO's guidelines. All liquidity policies and procedures are subject to review and approval by ALCO.

D2.2 Exposure to liquidity risk

The lending ratio, which is the ratio of total loans and advances to customer deposits and capital, is monitored on a daily basis in line with regulatory guidelines. Internally the lending ratio is set at a more conservative level than required by regulation. The Bank also manages its liquidity risk by monthly monitoring the liquid ratio, i.e. net liquid assets to total assets. For this purpose net liquid assets include cash and cash equivalents and investment grade debt securities for which there is an active and liquid market. Last year, the Bank has taken a number of initiatives to increase customer deposits progressively.

Details of the reported lending and liquid ratio as at 31 December 2018 were as follows:

	31 December 2018		31 December 2017	
	Lending ratio	**Liquid ratio**	Lending ratio	Liquid ratio
Average for the year	**78.00%**	**22.71%**	83.14%	23.49%
Maximum for the year	**79.17%**	**24.83%**	84.80%	27.40%
Minimum for the year	**76.21%**	**20.28%**	81.54%	17.04%

Bank also monitors the liquidity through Liquidity Coverage ratio (LCR) and Net Stable Funding Ratio (NSFR). Current levels of these ratios are given below

31 December 2018		31 December 2017	
LCR	**NSFR**	LCR	NSFR
215.40%	**106.18%**	213.53%	91.30%

D Financial risk management (continued)

D2 Liquidity risk (continued)

D2.2 Exposure to liquidity risk (continued)

The Liquidity Coverage ratio (LCR) and Net Stable Funding Ratio (NSFR) is calculated in accordance with Basel III framework and guidelines adopted by CBO vide circular BM 1127 and BM 1147. The complete disclosures required under these circulars are available on the Investor Relations page of the Bank's website.

The table below summarises the maturity profile of the Bank's liabilities as on the reporting date based on contractual repayment arrangements. The contractual maturities of liabilities have been determined on the basis of the remaining period at the statement of financial position date to the contractual maturity date and do not take account of the effective maturities as indicated by the Bank's deposit retention history and the availability of liquid funds.

	Carrying amount RO'000	**Gross nominal outflow RO'000**	**Within 3 months RO'000**	**3 - 12 months RO'000**	**Over 1 year RO'000**
31 December 2018					
Non – derivative liabilities					
Due to banks and other money market borrowings	**722,061**	**731,335**	**111,094**	**218,595**	**401,646**
Customers' deposits	**1,818,353**	**1,970,967**	**1,032,784**	**494,711**	**443,472**
Other liabilities	**84,664**	**84,664**	**84,664**	**-**	**-**
Subordinated loans	**35,392**	**46,318**	**366**	**2,084**	**43,868**
Compulsorily convertible bonds	**-**	**-**	**-**	**-**	**-**
Certificate of deposits	**509**	**509**	**-**	**-**	**509**
Total	**2,660,979**	**2,833,793**	**1,228,908**	**715,390**	**889,495**

	Carrying amount RO'000	Gross nominal outflow RO'000	Within 3 months RO'000	3 - 12 months RO'000	Over 1 year RO'000
31 December 2017					
Non – derivative liabilities					
Due to banks and other money market borrowings	718,619	746,466	183,305	198,129	365,032
Customers' deposits	1,642,845	1,756,980	872,311	427,479	457,190
Other liabilities	31,451	31,451	31,451	-	-
Subordinated loans	35,392	48,768	366	2,084	46,318
Compulsorily convertible bonds	2,402	2,437	-	2,437	-
Certificate of deposits	18,513	19,319	12	18,736	571
Total	2,449,222	2,605,421	1,087,445	648,865	869,111

D Financial risk management (continued)

D2 Liquidity risk (continued)

D2.2 Exposure to liquidity risk (continued)

	Carrying amount	**Gross Nominal Outflow**	**Within 3 months**	**3 - 12 months**	**Over 1 year**
	USD'000	**USD'000**	**USD'000**	**USD'000**	**USD'000**
31 December 2018					
Non – derivative liabilities					
Due to banks and other money market borrowings	**1,875,483**	**1,899,571**	**288,556**	**567,779**	**1,043,236**
Customers' deposits	**4,722,995**	**5,119,395**	**2,682,556**	**1,284,964**	**1,151,875**
Other liabilities	**219,907**	**219,907**	**219,907**	**-**	**-**
Subordinated loans	**91,927**	**120,306**	**950**	**5,413**	**113,943**
Compulsorily convertible bonds	**-**	**-**	**-**	**-**	**-**
Certificate of deposits	**1,322**	**1,322**	**-**	**-**	**1,322**
Total	**6,911,634**	**7,360,501**	**3,191,969**	**1,858,156**	**2,310,376**

	Carrying amount	Gross Nominal Outflow	Within 3 months	3 - 12 months	Over 1 year
	USD'000	USD'000	USD'000	USD'000	USD'000
31 December 2017					
Non – derivative liabilities					
Due to banks and other money market borrowings	1,866,543	1,938,873	476,117	514,621	948,135
Customers' deposits	4,267,130	4,563,584	2,265,743	1,110,335	1,187,506
Other liabilities	81,692	81,692	81,692	-	-
Subordinated loans	91,927	126,670	951	5,413	120,306
Compulsorily convertible bonds	6,239	6,330	-	6,330	-
Certificate of deposits	48,086	50,179	31	48,665	1,483
Total	6,361,617	6,767,328	2,824,534	1,685,364	2,257,431

The Bank prepares a liquidity gap report to monitor the Bank's short term liquidity position on its Rial denominated assets and liabilities in a time horizon spanning one month. The gap is adjusted for availability of instruments for repo or refinance and also for un-availed committed lines of credit, if any. This statement is reported to the ALCO monthly.

D Financial risk management (continued)

D3 Market risk

Market risk is the exposure to loss resulting from the changes in the interest rates, foreign currency exchange rates, equity prices and commodity prices. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return to risk.

D3.1 Measurement of market risk

The Bank is mainly engaged in spots transactions, forwards and currency swaps. Positions are mainly customer driven, which further reduces complexity. Accordingly, the Bank measures and controls its risk basically by using a limit framework. As and when the Bank enters into more complex derivatives, it has sophisticated models and techniques to measure market risk, supported by suitable controls.

D3.2 Management of market risks

The Bank separates its exposure to market risk between trading and non-trading portfolios. Trading portfolios include all positions arising from market making and proprietary position taking, together with financial assets and liabilities that are managed on a fair value basis.

All foreign exchange risk within the Bank is transferred by Treasury to the trading book. Accordingly, the foreign exchange position is treated as a part of the Bank's trading portfolio for risk management purposes. Foreign exchange risk is monitored and reported by Middle Office. The risk is managed through the Market Risk Management Policy by implementing a limit framework and reporting tools like Currency Position Report, Risk Analysis of Currency Position, Breach Analysis Report, and Dealer Limit Breach report.

Overall authority for market risk is vested in ALCO. The risk management function is responsible for development of detailed risk management policies (subject to approval by ALCO and BRC). The Market Risk Policy is periodically reviewed to keep it up to date with the market developments.

D3.3 Exposure to interest rate risk – non trading portfolios

Interest rate risk arises from the possibility that changes in interest rates will affect future profitability or the fair values of financial instruments. The Bank is exposed to interest rate risk as a result of mismatches of interest rate and re-pricing tenure of rate sensitive assets and liabilities.

The effective interest rate (effective yield) of a monetary financial instrument is the rate used in a present value calculation which results in the carrying amount of the instrument. The rate is a historical rate for a fixed rate instrument carried at amortised cost and a current rate for a floating rate instrument or an instrument carried at fair value.

The principal risk to which non-trading portfolios are exposed is the risk of loss from fluctuations in the future cash flows or fair values of financial instrument because of a change in market interest rates. Interest rate risk is managed principally through monitoring interest rate gaps. ALCO monitors compliance with these limits and is assisted by Risk Management in its day-to-day monitoring activities. A summary of the Bank's interest rate gap position on non-trading portfolios is provided in this note. As per Basel-II guidelines and communicated by CBO the Bank also assesses interest rate risk by assessing the impact on earnings and economic values of an interest rate shock of 200 bps and takes appropriate measures to reduce the impact. Additionally the Bank also assesses the impact on earnings of an interest rate shock of 50 and 100 bps.

D Financial risk management (continued)

D3 Market risk (continued)

D3.3 Exposure to interest rate risk – non trading portfolios (continued)

The Bank's interest sensitivity position based on contractual re-pricing arrangements at 31 December 2018 was as follows:

	Effective annual interest rate %	Within three months RO'000	Four months to 12 months RO'000	Over one year RO'000	Non-sensitive to interest rate RO'000	Total RO'000
31 December 2018						
Assets						
Cash and balances with Central Banks	**0.01**	**-**	**-**	**505**	**71,951**	**72,456**
Due from banks and other money market placements	**4.15**	**106,352**	**1,540**	**-**	**13,511**	**121,403**
Loans, advances and financing, net	**5.38**	**1,007,253**	**401,231**	**825,263**	**18,183**	**2,251,930**
Investments	**2.86**	**331,233**	**31,014**	**135,204**	**35,318**	**532,769**
Property, equipment and fixtures	**-**	**-**	**-**	**-**	**19,676**	**19,676**
Investment properties	**-**	**-**	**-**	**-**	**2,900**	**2,900**
Other assets	**-**	**-**	**-**	**-**	**45,269**	**45,269**
Total assets		**1,444,838**	**433,785**	**960,972**	**206,808**	**3,046,403**
Liabilities and equity						
Due to banks and other money market borrowings	**3.73**	**531,454**	**182,875**	**-**	**7,732**	**722,061**
Customers' deposits	**2.68**	**271,725**	**406,962**	**366,340**	**773,326**	**1,818,353**
Other liabilities	**-**	**-**	**-**	**-**	**84,664**	**84,664**
Subordinated loans	**7.00**	**-**	**-**	**35,000**	**392**	**35,392**
Compulsorily convertible bonds	**-**	**-**	**-**	**-**	**-**	**-**
Certificate of deposits	**4.75**	**-**	**-**	**500**	**9**	**509**
Total Equity	**-**	**-**	**-**	**-**	**385,424**	**385,424**
Total liabilities and equity		**803,179**	**589,837**	**401,840**	**1,251,547**	**3,046,403**
Gap		**641,659**	**(156,052)**	**559,132**	**(1,044,739)**	**-**
Cumulative Gap		**641,659**	**485,607**	**1,044,739**	**-**	**-**

D Financial risk management (continued)

D3 Market risk (continued)

D3.3 Exposure to interest rate risk – non trading portfolios (continued)

	Effective annual interest rate %	Within three months	Four months to 12 months	Over one year	Non-sensitive to interest rate	Total
		RO'000	RO'000	RO'000	RO'000	RO'000
31 December 2017						
Assets						
Cash and balances with Central Banks	0.01	-	-	505	181,819	182,324
Due from banks and other money market placements	2.51	72,165	-	-	32,038	104,203
Loans, advances and financing, net	5.17	864,822	409,297	820,755	3,874	2,098,748
Investments	2.33	254,900	44,249	94,759	19,833	413,741
Property, equipment and fixtures	-	-	-	-	17,109	17,109
Investment properties	-	-	-	-	2,900	2,900
Other assets	-	-	-	-	23,793	23,793
Total assets		1,191,887	453,546	916,019	281,366	2,842,818
Liabilities and equity						
Due to banks and other money market borrowings	2.91	594,800	90,075	-	33,744	718,619
Customers' deposits	2.64	188,147	384,616	375,842	694,240	1,642,845
Other liabilities	-	-	-	-	31,451	31,451
Subordinated loans	7.00	-	-	35,000	392	35,392
Compulsorily convertible bonds	4.50	-	2,383	-	19	2,402
Certificate of deposits	4.00	-	-	18,500	13	18,513
Total Equity	-	-	-	-	393,596	393,596
Total liabilities and equity		782,947	477,074	429,342	1,153,455	2,842,818
Gap		408,940	(23,528)	486,677	(872,089)	-
Cumulative Gap		408,940	385,412	872,089	-	-

D Financial risk management (continued)

D3 Market risk (continued)

D3.3 Exposure to interest rate risk – non trading portfolios (continued)

	Effective annual interest rate %	Within three months USD'000	Four months to 12 months USD'000	Over one year USD'000	Non-sensitive to interest rate USD'000	Total USD'000
31 December 2018						
Assets						
Cash and balances with Central Banks	0.01	-	-	1,311	186,886	188,197
Due from banks and other money market placements	4.15	276,239	4,000	-	35,093	315,332
Loans, advances and financing, net	5.38	2,616,243	1,042,158	2,143,539	47,229	5,849,169
Investments	2.86	860,345	80,556	351,179	91,736	1,383,816
Property, equipment and fixtures	-	-	-	-	51,107	51,107
Investment properties	-	-	-	-	7,532	7,532
Other assets	-	-	-	-	117,582	117,582
Total assets		3,752,827	1,126,714	2,496,029	537,165	7,912,735
Liabilities and equity						
Due to banks and other money market borrowings	3.73	1,380,400	475,000	-	20,083	1,875,483
Customers' deposits	2.68	705,779	1,057,044	951,533	2,008,639	4,722,995
Other liabilities	-	-	-	-	219,907	219,907
Subordinated loans	7.00	-	-	90,909	1,018	91,927
Compulsorily convertible bonds	-	-	-	-	-	-
Certificate of deposits	4.75	-	-	1,299	23	1,322
Total Equity	-	-	-	-	1,001,101	1,001,101
Total liabilities and equity		2,086,179	1,532,044	1,043,741	3,250,771	7,912,735
Gap		1,666,648	(405,330)	1,452,288	(2,713,606)	-
Cumulative Gap		1,666,648	1,261,318	2,713,606	-	-

D Financial risk management (continued)

D3 Market risk (continued)

D3.3 Exposure to interest rate risk – non trading portfolios (continued)

	Effective annual interest rate %	Within three months	Four months to 12 months	Over one year	Non-sensitive to interest rate	Total
		USD'000	USD'000	USD'000	USD'000	USD'000
31 December 2017						
Assets						
Cash and balances with Central Banks	0.01	-	-	1,312	472,257	473,569
Due from banks and other money market placements	2.51	187,442	-	-	83,215	270,657
Loans, advances and financing, net	5.17	2,246,291	1,063,109	2,131,831	10,063	5,451,294
Investments	2.33	662,078	114,932	246,127	51,515	1,074,652
Property, equipment and fixtures	-	-	-	-	44,439	44,439
Investment properties	-	-	-	-	7,532	7,532
Other assets	-	-	-	-	61,800	61,800
Total assets		3,095,811	1,178,041	2,379,270	730,821	7,383,943
Liabilities and equity						
Due to banks and other money market borrowings	2.91	1,544,935	233,961	-	87,647	1,866,543
Customers' deposits	2.64	488,694	999,003	976,213	1,803,220	4,267,130
Other liabilities	-	-	-	-	81,692	81,692
Subordinated loans	7.00	-	-	90,909	1,018	91,927
Compulsorily convertible bonds	4.50	-	6,190	-	49	6,239
Certificate of deposits	4.00	-	-	48,052	34	48,086
Total Equity	-	-	-	-	1,022,326	1,022,326
Total liabilities and equity		2,033,629	1,239,154	1,115,174	2,995,986	7,383,943
Gap		1,062,182	(61,113)	1,264,096	(2,265,165)	-
Cumulative Gap		1,062,182	1,001,069	2,265,165	-	-

D Financial risk management (continued)

D3 Market risk (continued)

D3.3 Exposure to interest rate risk – non trading portfolios (continued)

Interest rate risk is managed by taking views on interest rate movements for the year and realigning the portfolios and covenants of lending, so as to be proactive and minimise adverse effects. The benchmark presently available in Oman is the 28-day CBO CD rate. The trend of the weighted average interest on loans and cost of deposits for the year is provided below:

2018	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Lending rate	5.21%	5.19%	5.16%	5.17%	5.23%	5.24%	5.25%	5.28%	5.29%	5.30%	-	-
Deposit rate	1.67%	1.70%	1.64%	1.67%	1.70%	1.72%	1.73%	1.76%	1.79%	1.81%	-	-

2017	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Lending rate	5.10%	5.12%	5.12%	5.12%	5.13%	5.12%	5.16%	5.16%	5.19%	5.19%	5.22%	5.20%
Deposit rate	1.58%	1.59%	1.60%	1.60%	1.61%	1.62%	1.68%	1.67%	1.67%	1.67%	1.68%	1.67%

The management of interest rate risk is one of the critical components of market risk management in banks. Interest rate risk primarily arises on account of mismatch of the Bank's reprising assets with its reprising liabilities that fund the assets. There are basically two approaches to management of interest rate risk in banks, namely "Earnings Approach" and "Economic Value Approach". The interest rate risk is assessed based on the impact of interest rate shock on the Bank's earnings and capital.

The focus of earnings approach is understanding the impact of interest rate changes (shock) of assets and liabilities on the Net Interest Income of the Bank. It measures the extent of capability of the Bank to absorb decline in net interest income caused by interest rate changes.

Interest rate risk also influences the present value of the Bank's asset and liabilities. Economic value perspective considers the present value of the Bank's assets and liabilities and assesses the potential longer term impact of interest rates on the Bank. This perspective focuses on how the economic value of the Bank's assets and liabilities change with movements in interest rates and it reflects the impact of fluctuation in the interest rates on the economic value of the institution.

D Financial risk management (continued)

D3 Market risk (continued)

D3.3 Exposure to interest rate risk – non trading portfolios (continued)

The Basel-II Accord recommended that banks should assess the impact of interest rate risk by applying a 200 bps interest rate sensitivity and accordingly the impact of 200 bps interest rate shock on the Bank's earnings and capital is provided below:

31 December 2017 USD'000	31 December 2018 USD'000		31 December 2018 RO'000	31 December 2017 RO'000
133,750	159,244	Net interest income (including Islamic financing)	61,309	51,494
1,153,433	1,108,013	Total Regulatory Capital (note D5.1)	426,585	444,072
		Based on 50 bps interest rate shock		
4,995	6,460	Impact of 50 bps interest rate shock	2,487	1,923
3.73%	4.06%	Impact as % to net interest income	4.06%	3.73%
0.43%	0.58%	Impact as % to capital	0.58%	0.43%
		Based on 100 bps interest rate shock		
9,990	12,919	Impact of 100 bps interest rate shock	4,974	3,846
7.47%	8.11%	Impact as % to net interest income	8.11%	7.47%
0.87%	1.17%	Impact as % to capital	1.17%	0.85%
		Based on 200 bps interest rate shock		
19,719	25,839	Impact of 200 bps interest rate shock	9,948	7,692
14.94%	16.23%	Impact as % to net interest income	16.23%	14.94%
1.73%	2.33%	Impact as % to capital	2.33%	1.73%

D3.4 Exposure to other market risks

Investment value risk is the risk of reduction in the market value of the Bank's portfolio as a result of diminution in the market value of individual investments. The responsibility for management of investment value risk rests with the Investment division under the supervision and guidance of the Management Investment Committee and Board Executive Committee of the Bank. The Bank's investments are governed by an investment policy approved by the Board of Directors. The ratings and prices of the instruments are monitored on a regular basis and necessary actions are taken to reduce exposure if needed. The portfolio is revalued at market price to ensure that unrealised losses, if any, on account of reduction in the market value of the investments remains within acceptable parameters.

Security as per country	**Changes in fair value +/- 5%**	
	31 December 2018 RO'000	31 December 2017 RO'000
Organisation for Economic Co-operation (OECD) Countries	-	176
Oman	494	440
Other Gulf Co-operation Council (GCC) countries	5	5
	31 December 2018 USD'000	31 December 2017 USD'000
Organisation for Economic Co-operation (OECD) Countries	-	457
Oman	1,283	1,143
Other Gulf Co-operation Council (GCC) countries	13	13

D Financial risk management (continued)

D3 Market risk (continued)

D3.4 Exposure to other market risks (continued)

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Board has set limits on the total open position and open position per currency. The open position limits include overnight and intraday open position. Open positions are monitored on a daily basis and hedging strategies used to ensure positions are maintained within established limits. The Bank had the following net open positions denominated in foreign currencies:

	31 December 2018			31 December 2017		
	Assets FCY' 000	**Liabilities FCY' 000**	**Net (liabilities)/assets FCY' 000**	Assets FCY' 000	Liabilities FCY' 000	Net (liabilities)/assets FCY' 000
US Dollar	**2,752,642**	**3,004,388**	**(251,745)**	2,215,492	2,497,939	(282,447)
Euro	**147,316**	**147,298**	**18**	111,144	111,129	15
UAE Dirhams	**125,076**	**48,122**	**76,954**	171,370	317,969	(146,599)
Japanese Yen	**52,426**	**51,411**	**1,015**	9,000,000	9,016,897	(16,897)
Pound Sterling	**8,479**	**8,464**	**15**	4,777	4,750	27
Indian Rupee	**12,957**	**196**	**12,761**	7,796	86	7,710
Other currencies (in RO'000)			**888**			2,358

The Bank's open foreign currency positions are a result of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Board sets limits on the level of exposure by currency and in aggregate for both overnight and intra-day positions, which are monitored daily.

D4 Operational risk

Operational risk is defined as the risk of direct or indirect loss resulting from inadequate or failed internal processes, people, technology, infrastructure or from external events and excludes credit, market and liquidity risks.

The Bank's objective is to manage operational risk to avoid/reduce financial losses to the Bank by the establishment of the necessary controls, systems and procedures. The Bank recognises that an over-controlled environment will affect the Bank's business and earnings, besides adding to costs. Therefore, the Bank aims to effectively manage operational risk through control optimisation and well established systems, methods and governance framework.

The primary responsibility for development and implementation of controls to address operational risk is assigned to senior management within each business unit. This responsibility is supported by the development of overall Bank standards in the following areas:

- Clear reporting lines;
- Proper delegation of powers;
- Appropriate segregation of duties and authorisation of transactions through a maker checker system and authorisation matrix;
- Ownership reconciliation and monitoring of accounts;
- Documentation of controls and processes;
- Compliance with regulatory and other legal requirements;
- Periodic assessment of the operational risks faced and evaluating the adequacy of controls and procedures to address the risks identified;
- Reporting of operational losses and incidents triggering operational losses and remedial action;
- Development of contingency plans;
- Training, skill up gradation and professional development;
- Ethical and business standards; and
- Risk mitigation through insurance, wherever desirable.

D Financial risk management (continued)

D4 Operational risk (continued)

Compliance with Bank standards for both conventional and Islamic banking divisions is supported by a programme of periodic reviews undertaken by Internal Audit. The results of Internal Audit reviews are discussed with the management of the business unit to which they relate, with summaries submitted to the Audit Committee and management. The Bank also implemented a comprehensive Operational Risk Management Framework and put in place Operational Risk Management Policy, Risk and Control Self-Assessment (RCSA) Policy, Operational Risk Loss Event Reporting Framework, Maintenance of Operational Risk Loss Data Base and RCSA Framework. The Bank developed an in-house RCSA model and has conducted Risk and Control Self-Assessment for all major business activities like Corporate Banking, Retail Banking, Treasury, Card operations, Deposits, HR, E-banking, Administration, Branch operations, Compliance, Legal, IT, Credit Administration, Payment unit etc. The Bank further identified Key Risk Indicators (KRI) of operational risk in major activities of the Bank and set threshold limits that are monitored monthly to assess the level of risk and manage the same.

D5 Capital management

D5.1 Regulatory capital

The Bank's lead regulator, CBO, sets and monitors the capital requirements for the Bank as a whole. In implementing current capital requirements CBO requires the Bank to maintain a prescribed ratio of total capital to total risk-weighted assets. The Bank calculates capital requirements for market risk and operational risk based upon the model prescribed by CBO as follows:

- Claims against sovereign entities in the respective national currencies – Nil
- Claims against sovereign entities in other currencies – 100% risk weighting is applied as prescribed by CBO
- Retail and Corporate loans – In the absence of credit rating model 100% risk weighting is applied
- Off balance sheet items – As per credit conversion factors and risk weighting prescribed by CBO

The Bank's regulatory capital is analysed into two tiers:

- Tier 1 capital includes ordinary share capital, share premium, perpetual Tier 1 capital securities classified as innovative Tier 1 securities, retained earnings, translation reserve and minority interests after deductions for goodwill and intangible assets, and other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes.

- Tier 2 capital includes qualifying subordinated liabilities, collective impairment allowances and unrealised losses on equity instruments classified as available for sale investments.

Various limits are applied to elements of the capital base. The amount of innovative tier 1 securities cannot exceed 15 per cent of total tier 1 capital; qualifying tier 2 capital cannot exceed tier 1 capital; and qualifying term subordinated loan capital may not exceed 50 per cent of tier 1 capital. There are also restrictions on the amount of collective impairment allowances that may be included as part of tier 2 capital. Other deductions from capital include the carrying amounts of investments in subsidiaries that are not included in the regulatory consolidation, investments in the capital of banks and certain other regulatory items.

Banking operations are categorised as either trading book or banking book, and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and off-balance sheet exposures. The Bank's policy is to maintain a strong capital base to maintain investor, creditor and market confidence and to sustain future development of the business. The impact of the level of capital on shareholders' return is also recognised and the Bank recognises the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position.

D5 Capital management (continued)

D5.1 Regulatory capital (continued)

The international standard for measuring capital adequacy is the risk asset ratio, which relates capital to balance sheet assets and off balance sheet exposures weighted according to broad categories of risk.
The risk asset ratio calculated in accordance with the capital adequacy guidelines of the Bank for International Settlement is as follows:

31 December 2017 USD'000	**31 December 2018 USD'000**		**31 December 2018 RO'000**	31 December 2017 RO'000
		CET 1 capital		
463,545	**514,974**	Ordinary share capital	**198,265**	178,465
45,732	**46,849**	Share premium	**18,037**	17,607
55,683	**63,312**	Legal reserve	**24,375**	21,438
2,566	**2,566**	General reserve	**988**	988
-	**18,182**	Subordinated loan reserve	**7,000**	-
165,529	**70,096**	Retained earnings *	**26,987**	63,728
(2,036)	**(5,540)**	Fair value losses	**(2,133)**	(784)
731,017	**710,439**	**Total CET 1 capital**	**273,519**	281,442
		Additional Tier 1 capital		
259,740	**259,740**	Perpetual Tier 1 Capital Securities	**100,000**	100,000
990,757	**970,179**	**Total Tier 1 capital**	**373,519**	381,442
		Tier 2 capital		
65,421	**65,096**	Impairment allowance on portfolio basis	**25,062**	25,187
156	**10**	Fair value gains	**4**	60
90,909	**72,727**	Subordinated loan	**28,000**	35,000
6,190	**-**	Compulsorily convertible bonds	**-**	2,383
162,676	**137,833**	**Total Tier 2 capital**	**53,066**	62,630
1,153,433	**1,108,012**	**Total regulatory capital**	**426,585**	444,072
		Risk weighted assets		
6,746,257	**6,959,236**	Credit and market risks	**2,679,306**	2,597,309
363,912	**410,182**	Operational risk	**157,920**	140,106
7,110,169	**7,369,418**	**Total risk weighted assets**	**2,837,226**	2,737,415
		Capital adequacy ratio		
16.22%	**15.04%**	Total regulatory capital expressed as a percentage of total risk weighted assets	**15.04%**	16.22%
13.93%	**13.16%**	Total tier I capital expressed as a percentage of total risk weighted assets	**13.16%**	13.93%
10.28%	**9.64%**	Total CET 1 capital expressed as a percentage of total risk weighted assets	**9.64%**	10.28%

* Retained earnings for the year 2018 is stated after deducting cash dividend of RO 11,895,900 (2017: RO 8,923,250), as disclosed in B26.
The capital adequacy ratio is calculated in accordance with Basel II & Basel III requirements as adopted by CBO. Disclosures required under Basel III and circular BM-1114 dated 17 November 2013 issued by CBO are available on the Investor Relations page of the Bank's website.

E Segmental information

Segmental information is presented for the Bank's operating segments. For management purposes, the Bank is organised into six operating segments, excluding head office, based on products and services as follows:

- Wholesale banking includes loans to and deposits from corporates, small & medium enterprises and trade finance customers.
- Retail banking includes loans to and deposits from retail customers, credit card and fund transfer facilities.
- Government and project finance syndication include loans to and deposits from government and financial institutions, project finance and syndicated loans.
- Investments include proprietary investments, correspondent and investment banking.
- Treasury principally includes money market instruments, derivative and foreign exchange products.
- Head office includes balance sheet, income and expense related items that are not directly related to the Bank's operating segments.
- Islamic banking includes Islamic financing activities, current accounts, unrestricted investment accounts and other products and services to corporate and individual customers under Shari'a principles.

The CEO monitors the operating results of business units separately for the purpose of making decisions about resource allocation and performance assessment. Interest income is reported net as the CEO primarily relies on net interest income as a performance measure, not the gross income and expense.

Transfer pricing between operating segments is on an arm's length basis in a manner similar to transactions with third parties.

No revenue from transactions with a single external counterparty or customer amounted to 10% or more of the Bank's total revenue in 2018 or 2017.

E1 Segmental information (continued)

31 December 2018	*Retail banking RO'000*	*Wholesale banking RO'000*	*Government institution & PFS* RO'000*	*Investments &FI RO'000*	*Treasury RO'000*	*Head Office RO'000*	*Islamic banking RO'000*	*Total RO'000*
Income Statement								
Interest income	37,280	58,598	17,520	941	15,984	-	-	**130,323**
Interest expense	(17,543)	(36,023)	(11,404)	(1,203)	(7,499)	-	-	**(73,672)**
Net interest income	19,737	22,575	6,116	(262)	8,485	-	-	**56,651**
Net income from Islamic financing and investing activities	-	-	-	-	-	-	4,658	**4,658**
Other operating income	4,909	9,507	2,886	1,976	13,228	-	623	**33,129**
Total Operating income	24,646	32,082	9,002	1,714	21,713	-	5,281	**94,438**
Total Operating expenses	(20,672)	(8,568)	(1,776)	(1,876)	(2,267)	(1,100)	(3,626)	**(39,885)**
Net Operating Income	3,974	23,514	7,226	(162)	19,446	(1,100)	1,655	**54,553**
Impairment on available for sale investments	-	-	-	(314)	(336)	-	(31)	**(681)**
Loan impairment charges and other credit risk provisions, net	(2,846)	(13,068)	(1,188)	(922)	(426)	-	(992)	**(19,442)**
Segment profit / (loss)	1,128	10,446	6,038	(1,398)	18,684	(1,100)	632	**34,430**
Income tax expense	(169)	(1,567)	(906)	310	(2,802)	165	(95)	**(5,064)**
Profit / (loss) for the year	959	8,879	5,132	(1,088)	15,882	(935)	537	**29,366**
Balance sheet								
Assets								
Cash and balances with Central Bank	-	-	-	-	63,719	-	8,737	**72,456**
Due from banks and other money market placements	-	-	8,240	-	103,333	-	9,830	**121,403**
Loans, advances and financing, net	674,975	1,037,562	359,027	-	-	-	180,366	**2,251,930**
Investments	-	-	-	20,845	490,980	-	20,944	**532,769**
Property, equipment and fixtures	-	-	-	-	-	18,550	1,126	**19,676**
Investment properties	-	-	-	-	-	2,900	-	**2,900**
Other assets	-	30,252	-	-	1,883	11,936	1,198	**45,269**
TOTAL ASSETS	674,975	1,067,814	367,267	20,845	659,915	33,386	222,201	**3,046,403**
Liabilities								
Due to banks and other money market borrowings	-	-	-	-	709,358	-	12,703	**722,061**
Customers' deposits	374,609	278,024	817,970	58,414	108,511	-	180,825	**1,818,353**
Other liabilities	-	30,252	20,000	-	3,702	29,057	1,653	**84,664**
Subordinated loans	-	-	-	-	-	35,392	-	**35,392**
Compulsorily convertible bonds	-	-	-	-	-	-	-	**-**
Certificate of deposits	-	-	-	-	509	-	-	**509**
TOTAL LIABILITIES	374,609	308,276	837,970	58,414	822,080	64,449	195,181	**2,660,979**
TOTAL EQUITY	-	-	-	-	-	357,942	27,482	**385,424**
	374,609	308,276	837,970	58,414	822,080	422,391	222,663	**3,046,403**

* Financial Institutions & Project Finance and Syndication

E1 Segmental information (continued)

	Retail banking	*Wholesale banking*	*Government institution & PFS**	*Investments &FI*	*Treasury*	*Head Office*	*Islamic banking*	*Total*
31 December 2017	*RO'000*	*RO'000*	*RO'000*	*RO'000*	*RO'000*	*RO'000*	*RO'000*	*RO'000*
Income Statement								
Interest income	33,591	54,096	11,971	1,082	8,535	-	-	109,275
Interest expense	(16,143)	(30,906)	(7,661)	(542)	(6,302)	-	-	(61,554)
Net interest income	17,448	23,190	4,310	540	2,233	-	-	47,721
Net income from Islamic financing and investing activities	-	-	-	-	-	-	3,773	3,773
Other operating income	4,336	14,911	2,607	588	1,702	-	778	24,922
Total Operating income	21,784	38,101	6,917	1,128	3,935	-	4,551	76,416
Total Operating expenses	(18,728)	(7,634)	(1,477)	(2,046)	(2,099)	-	(2,814)	(34,798)
Net Operating Income	3,056	30,467	5,440	(918)	1,836	-	1,737	41,618
Impairment on available for sale investments	-	-	-	(1,956)	-	-	-	(1,956)
Loan impairment charges and other credit risk provisions, net	(2,709)	(4,209)	(966)	-	-	(1,109)	(734)	(9727)
Segment profit / (loss)	347	26,258	4,474	(2,874)	1,836	(1,109)	1,003	29,935
Income tax expense	(52)	(3,939)	(671)	317	(275)	166	(150)	(4,604)
Profit / (loss) for the year	295	22,319	3,803	(2,557)	1,561	(943)	853	25,331
Balance sheet								
Assets								
Cash and balances with Central Bank	-	-	-	-	167,102	-	15,222	182,324
Due from banks and other money market placements	-	-	21,486	-	74,735	-	7,982	104,203
Loans, advances and financing, net	595,493	1,067,454	290,289	-	-	-	145,512	2,098,748
Investments	-	-	-	20,992	376,945	-	15,804	413,741
Property, equipment and fixtures	-	-	-	-	-	16,013	1,096	17,109
Investment properties	-	-	-	-	-	2,900	-	2,900
Other assets	-	9,847	-	-	1,744	11,137	1,065	23,793
TOTAL ASSETS	595,493	1,077,301	311,775	20,992	620,526	30,050	186,681	2,842,818
Liabilities								
Due to banks and other money market borrowings	-	-	-	-	718,619	-	-	718,619
Customers' deposits	375,546	306,940	722,244	11,864	63,487	-	162,764	1,642,845
Other liabilities	-	9,847	-	-	898	19,748	958	31,451
Subordinated loans	-	-	-	-	-	35,392	-	35,392
Compulsorily convertible bonds	-	-	-	-	-	2,402	-	2,402
Certificate of deposits	-	-	-	-	18,513	-	-	18,513
TOTAL LIABILITIES	375,546	316,787	722,244	11,864	801,517	57,542	163,722	2,449,222
TOTAL EQUITY	-	-	-	-	-	370,578	23,018	393,596
	375,546	316,787	722,244	11,864	801,517	428,120	186,740	2,842,818

* Financial Institutions & Project Finance and Syndication

E1 Segmental information (continued)

31 December 2018	*Retail banking USD'000*	*Wholesale banking USD'000*	*Government institution, FI & PFS* USD'000*	*Investments USD'000*	*Treasury USD'000*	*Head Office USD'000*	*Islamic banking USD'000*	*Total USD'000*
Income Statement								
Interest income	96,831	152,203	45,506	2,444	41,517	-	-	**338,501**
Interest expense	(45,566)	(93,566)	(29,621)	(3,125)	(19,478)	-	-	**(191,356)**
Net interest income	51,265	58,637	15,885	(681)	22,039	-	-	**147,145**
Net income from Islamic financing and investing activities	-	-	-	-	-	-	12,099	**12,099**
Other operating income	12,751	24,694	7,496	5,132	34,358	-	1,618	**86,049**
Total Operating income	64,016	83,331	23,381	4,451	56,397		13,717	**245,293**
Total Operating expenses	(53,693)	(22,255)	(4,613)	(4,873)	(5,888)	(2,857)	(9,418)	**(103,597)**
Net Operating Income	10,323	61,076	18,768	(422)	50,509	(2,857)	4,299	**141,696**
Impairment on available for sale investments	-	-	-	(816)	(873)	-	(80)	**(1,769)**
Loan impairment charges and other credit risk provisions, net	(7,392)	(33,943)	(3,086)	(2,395)	(1,106)	-	(2,577)	**(50,499)**
Segment profit / (loss)	2,931	27,133	15,682	(3,633)	48,530	(2,857)	1,642	**89,428**
Income tax expense	(439)	(4,070)	(2,353)	805	(7,278)	429	(247)	**(13,153)**
Profit / (loss) for the year	2,492	23,063	13,329	(2,828)	41,252	(2,428)	1,395	**76,275**
Balance sheet								
Assets								
Cash and balances with Central Bank	-	-	-	-	165,504	-	22,693	**188,197**
Due from banks and other money market placements	-	-	21,403	-	268,397	-	25,532	**315,332**
Loans, advances and financing, net	1,753,182	2,694,966	932,538	-	-	-	468,483	**5,849,169**
Investments	-	-	-	54,143	1,275,273	-	54,400	**1,383,816**
Property, equipment and fixtures	-	-	-	-	-	48,182	2,925	**51,107**
Investment properties	-	-	-	-	-	7,532	-	**7,532**
Other assets	-	78,577	-	-	4,891	31,002	3,112	**117,582**
TOTAL ASSETS	1,753,182	2,773,543	953,941	54,143	1,714,065	86,716	577,145	**7,912,735**
Liabilities								
Due to banks and other money market borrowings	-	-	-	-	1,842,488	-	32,995	**1,875,483**
Customers' deposits	973,010	722,140	2,124,598	151,725	281,847	-	469,675	**4,722,995**
Other liabilities		78,577	51,948	-	9,616	75,472	4,294	**219,907**
Subordinated loans	-	-	-	-	-	91,927	-	**91,927**
Compulsorily convertible bonds	-	-	-	-	-	-	-	**-**
Certificate of deposits	-	-	-	-	1,322	-	-	**1,322**
TOTAL LIABILITIES	973,010	800,717	2,176,546	151,725	2,135,273	167,399	506,964	**6,911,634**
TOTAL EQUITY	-	-	-	-	-	929,719	71,382	**1,001,101**
	973,010	800,717	2,176,546	151,725	2,135,273	1,097,118	578,346	**7,912,735**

* Financial Institutions & Project Finance and Syndication

E1 Segmental information (continued)

31 December 2017	*Retail banking USD'000*	*Wholesale banking USD'000*	*Government institution, FI & PFS* USD'000*	*Investments USD'000*	*Treasury USD'000*	*Head Office USD'000*	*Islamic banking USD'000*	*Total USD'000*
Income Statement								
Interest income	87,249	140,509	31,094	2,810	22,169	-	-	283,831
Interest expense	(41,930)	(80,275)	(19,899)	(1,408)	(16,369)	-	-	(159,881)
Net interest income	45,319	60,234	11,195	1,402	5,800	-	-	123,950
Net income from Islamic financing and investing activities	-	-	-	-	-	-	9,800	9,800
Other operating income	11,262	38,730	6,772	1,527	4,421	-	2,021	64,733
Total Operating income	56,581	98,964	17,967	2,929	10,221	-	11,821	198,483
Total Operating expenses	(48,644)	(19,829)	(3,836)	(5,314)	(5,452)	-	(7,309)	(90,384)
Net Operating Income	7,937	79,135	14,131	(2,385)	4,769	-	4,512	108,099
Impairment on available for sale investments	-	-	-	(5,081)	-	-	-	(5,081)
Loan impairment charges and other credit risk provisions, net	(7,036)	(10,932)	(2,509)	-	-	(2,881)	(1,906)	(25,264)
Segment profit / (loss)	901	68,203	11,622	(7,466)	4,769	(2,881)	2,606	77,754
Income tax expense	(135)	(10,231)	(1,742)	823	(714)	431	(390)	(11,958)
Profit / (loss) for the year	766	57,972	9,880	(6,643)	4,055	(2,450)	2,216	65,796
Balance sheet								
Assets								
Cash and balances with Central Bank	-	-	-	-	434,031	-	39,538	473,569
Due from banks and other money market placements	-	-	55,808	-	194,117	-	20,732	270,657
Loans, advances and financing, net	1,546,735	2,772,608	753,998	-	-	-	377,953	5,451,294
Investments	-	-	-	54,525	979,078	-	41,049	1,074,652
Property, equipment and fixtures	-	-	-	-	-	41,592	2,847	44,439
Investment properties	-	-	-	-	-	7,532	-	7,532
Other assets	-	25,577	-	-	4,530	28,927	2,766	61,800
TOTAL ASSETS	1,546,735	2,798,185	809,806	54,525	1,611,756	78,051	484,885	7,383,943
Liabilities								
Due to banks and other money market borrowings	-	-	-	-	1,866,543	-	-	1,866,543
Customers' deposits	975,444	797,247	1,875,958	30,816	164,901	-	422,764	4,267,130
Other liabilities	-	25,577	-	-	2,333	51,294	2,488	81,692
Subordinated loans	-	-	-	-	-	91,927	-	91,927
Compulsorily convertible bonds	-	-	-	-	-	6,239	-	6,239
Certificate of deposits	-	-	-	-	48,086	-	-	48,086
TOTAL LIABILITIES	975,444	822,824	1,875,958	30,816	2,081,863	149,460	425,252	6,361,617
TOTAL EQUITY	-	-	-	-	-	962,539	59,787	1,022,326
	975,444	822,824	1,875,958	30,816	2,081,863	1,111,999	485,039	7,383,943

* Financial Institutions & Project Finance and Syndication

E2 Comparative figures

Certain comparative figures for 2017 have been reclassified in order to conform to the presentation for the current period. Such reclassifications do not affect previously reported net profit or shareholders' equity.

SOHAR ISLAMIC
(ISLAMIC BANKING WINDOW OF SOHAR INTERNATIONAL BANK SAOG)

FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018

Registered office and principal place of business:

Bank Sohar Building
P.O. Box 44, Hai Al-Mina
PC 114, Muscat
Sultanate of Oman

SOHAR ISLAMIC
(ISLAMIC BANKING WINDOW OF SOHAR INTERNATIONAL BANK SAOG)

FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018

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EY
Building a better working world

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PR No. HMH/15/2015; HMA/9/2015

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF SOHAR INTERNATIONAL BANK SAOG (PREVIOUSLY "BANK SOHAR SAOG") ("THE BANK")

Report on the financial statements

We have audited the accompanying statement of financial position of Sohar Islamic (the "Islamic Window") as of 31 December 2018, and the related statements of income, changes in owners' equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information. These financial statements and the Bank's undertaking to operate its Islamic Window in accordance with Islamic Shari'a Rules and Principles as determined by the Shari'a Supervisory Board are the responsibility of the Bank's Board of Directors. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Auditing Standards for Islamic Financial Institutions issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ("AAOIFI"). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Islamic Window as of 31 December 2018, the results of its operations, cash flows and changes in equity for the year then ended in accordance with the Shari'a Rules and Principles as determined by the Shari'a Supervisory Board of the Islamic Window of the Bank and the Financial Accounting Standards issued by AAOIFI.

Ernst & Young LLC

إرنست ويونغ ش م م
س.ت: ١٢٢٤٠١٣
ص.ب: ١٧٥٠ روي - ١١٢، سلطنة عمان
EY ERNST & YOUNG LLC
C.R. No. 1224013
P.O. Box 1750 - P.C. 112, Sultanate of Oman

12 March 2019
Muscat

SOHAR ISLAMIC
(ISLAMIC BANKING WINDOW OF SOHAR INTERNATIONAL BANK SAOG)

STATEMENT OF FINANCIAL POSITION
AS AT 31 DECEMBER 2018

	Note	31 December 2018 RO'000	31 December 2017 RO'000
ASSETS			
Cash and balances with central bank	B 1	**8,737**	15,222
Due from banks and financial institutions	B 2	**9,830**	7,982
Murabaha receivables	B 3A	**13,360**	12,250
Ijarah muntahia bittamleek	B 3B	**57,049**	54,228
Istisna followed by Ijarah muntahia bittamleek	B 3C	**73,904**	41,000
Diminishing Musharka	B 3D	**35,311**	37,444
Investment securities	B 4	**20,944**	15,804
Property, equipment and fixture	B 5	**1,126**	1,097
Other assets	B 6	**2,404**	1,713
TOTAL ASSETS		**222,665**	186,740
LIABILITIES			
Wakala deposits	B 7	**133,376**	108,461
Customer deposit and other accounts	B 8	**19,168**	19,836
Other liabilities	B 9	**1,655**	957
TOTAL LIABILITIES		**154,199**	129,254
EQUITY OF INVESTMENT ACCOUNT HOLDERS	B 10	**40,984**	34,467
EQUITY			
Assigned capital	B 11 (a)	**25,000**	21,000
Legal reserve	B 11 (b)	**134**	134
General reserve	B 11 (c)	**988**	988
Retained earnings		**1,360**	897
TOTAL OWNERS' EQUITY		**27,482**	23,019
TOTAL LIABILITIES, EQUITY OF INVESTMENT ACCOUNT HOLDERS AND OWNERS' EQUITY		**222,665**	186,740
CONTINGENT LIABILITIES	B15.1	**32,301**	26,229
COMMITMENTS	B15.2	**1,045**	6,341

These financial statements were approved and authorised for issue by the Board of Directors on 30 January 2019 and signed on their behalf by:

Chairman **Deputy Chairman**

The accompanying notes A1 to D8 form part of these financial statements.

SOHAR ISLAMIC
(ISLAMIC BANKING WINDOW OF SOHAR INTERNATIONAL BANK SAOG)

STATEMENT OF INCOME
FOR THE YEAR ENDED 31 DECEMBER 2018

	Note	31 December 2018 RO'000	31 December 2017 RO'000
Income from jointly financed financing activities and receivables	C 1	**2,252**	1,992
Return on unrestricted investment account holders	C3	**(744)**	(392)
Share of income (as Mudarib and Rabalmal)		**1,508**	1,600
Income from self-financed financing activities	C 1	**6,184**	4,549
Income from self-financed investing activities	C 2	**1,135**	683
Income from financing, investments and receivables		**8,827**	6,832
Return on due to under Wakala contracts	C3	**(4,170)**	(3,059)
Net revenue from financing and investing activities		**4,657**	3,773
Other income	C4	**263**	476
Foreign exchange gain – net		**360**	302
Total revenues		**5,280**	4,551
Staff costs		**(1,891)**	(1,547)
Other operating expenses	C 5	**(1,441)**	(985)
Depreciation	B 5	**(293)**	(282)
Total expenses		**(3,625)**	(2,814)
Operating profit		**1,655**	1,737
Expected credit loss on investment securities	B 4	**(21)**	-
Expected credit loss on due from banks and financial institutions	B 2	**(10)**	-
Expected credit loss on financing advances and other receivables	B 3	**(986)**	-
Expected credit loss on financing advance commitments and financial guarantees	B 9	**(6)**	-
Portfolio impairment allowances		**-**	(636)
Specific impairment allowances, net		**-**	(98)
Profit for the year before tax		**632**	1,003
Tax allocated from head office		**(95)**	(150)
Profit for the year after tax		**537**	853

The accompanying notes A1 to D8 form part of these financial statements.

SOHAR ISLAMIC
(ISLAMIC BANKING WINDOW OF SOHAR INTERNATIONAL BANK SAOG)

STATEMENT OF OWNERS' EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2018

	Note	Allocated capital RO'000	Legal reserve RO'000	General reserve RO'000	Retained earnings RO'000	Total RO'000
Balance as at 1 January		**21,000**	**134**	**988**	**897**	**23,019**
Impact of adopting IFRS 9	A 5 (i)	**-**	**-**	**-**	**(74)**	**(74)**
Restated opening balance under IFRS 9		**21,000**	**134**	**988**	**823**	**22,945**
Capital allocated during the year	B 11 (a)	**4,000**	**-**	**-**	**-**	**4,000**
Profit for the year		**-**	**-**	**-**	**537**	**537**
Balance as at 31 December		**25,000**	**134**	**988**	**1,360**	**27,482**

	Note	Assigned capital RO'000	Legal reserve RO'000	General reserve RO'000	Retained earnings RO'000	Total RO'000
Balance as at 1 January 2017		17,000	134	988	44	18,166
Capital allocated during the year	B 11 (a)	4,000	-	-	-	4,000
Profit for the year		-	-	-	853	853
Balance as at 31 December 2017		21,000	134	988	897	23,019

The accompanying notes A1 to D8 form part of these financial statements.

SOHAR ISLAMIC
(ISLAMIC BANKING WINDOW OF SOHAR INTERNATIONAL BANK SAOG)

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2018

	31 December 2018 RO'000	31 December 2017 RO'000
Cash flows from operating activities		
Profit before taxation	**632**	1,003
Adjustments for:		
Depreciation	**293**	282
Net impairment loss on financing assets	**1,023**	734
Revaluation gain on investments	**-**	18
Loss on disposal of fixed assets	**7**	-
Income on investments	**(930)**	(614)
Operating profit before changes in operating assets and liabilities	**1,025**	1,274
Changes in operating assets and liabilities		
Murabaha receivables	**(996)**	(4,540)
Ijarah muntahia bittamleek	**(2,788)**	(9,536)
Istisna followed by Ijarah muntahia bittamleek	**(33,075)**	(20,953)
Diminishing Musharka	**984**	(15,062)
Wakala deposits	**12,212**	57,320
Customer deposit and other accounts	**(668)**	6,786
Other assets	**(537)**	(157)
Other liabilities	**698**	(253)
Income tax paid	**(112)**	(133)
Net cash (used in) / from operating activities	**(23,257)**	14,896
Cash flows used in investing activities		
Acquisition of fixed assets	**(380)**	(85)
Disposal of fixed assets	**50**	-
Income received on Investments	**644**	590
Disposal of Investments	**8,000**	-
Acquisition of Investments	**(12,899)**	(5,775)
Net cash used in investing activities	**(4,585)**	(5,270)
Cash flows from financing activities		
Changes in URIA	**6,517**	249
Capital allocated during the year	**4,000**	4,000
Net cash from financing activities	**10,517**	4,249
Net (decrease) / increase in cash and cash equivalents	**(17,325)**	13,875
Cash and cash equivalent at beginning of the year	**23,204**	9,329
Cash and cash equivalents at 31 December	**5,879**	23,204
REPRESENTING:		
Cash and balances with Central Bank	**8,737**	15,222
Due from banks and financial institutions	**9,845**	7,982
Wakala deposits from banks	**(12,703)**	-
	5,879	23,204

The accompanying notes A1 to D8 form part of these financial statements.

A1 INCORPORATION, LEGAL STATUS AND PRINCIPAL ACTIVITIES

Sohar International Bank SAOG (the Head office) (previously 'Bank Sohar SAOG) under an Islamic Banking License issued by the Central Bank of Oman (CBO) on 30 April 2013, carries out Islamic banking operations and other financial trading activities in accordance with Islamic Shari'a rules and regulations under the name of "Sohar Islamic" (the Window). The Bank's Shari'a Supervisory Board is entrusted to ensure the Window's adherence to Shari'a rules and principles in its transactions and activities. As required under clauses 3.5.1.2 and 3.5.1.3 of Title 1,'*Licensing Requirements*' of Islamic Banking Regulatory Framework (IBRF) issued by CBO, the head office assigned RO 25 million (refer note B14a) to the Window as assigned capital.

The Window offers a full range of Islamic banking services and products. The principal activities of the Window include accepting Shari'a compliant customer deposits, providing Shari'a compliant financing and undertaking investment activities and providing commercial banking services and other investment activities permitted under IBRF.

A2 BASIS OF PREPARATION

A2.1 Statement of compliance

The financial statements for the Window are prepared in accordance with the Financial Accounting Standards (FAS) issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ("AAOIFI"), the Islamic Shari'a rules and principles as determined by the Shari'a Supervisory Board of the Window and Islamic Banking Regulatory Framework issued by CBO. In accordance with the requirement of AAOIFI, for matters not covered by FAS, the Window uses standards issued by the International Accounting Standards Board (IASB) and the interpretations released by the International Financial Reporting Interpretations Committee and will be replaced later by FAS when an applicable FAS is issued.

The Window has not operated as a separate legal entity. The separate financial statements of the Window has been prepared to comply with the requirement of Articles 1.5.1.2 to 1.5.1.4 of Title 2 'General Obligations and Governance' of IBRF issued by CBO.

Statement of sources and uses of charity fund are not presented as these are not applicable.

A2.2 Basis of measurement

The financial statements have been prepared under the historical cost basis except for derivative financial instruments and investment which has been measured at fair value. These financial statements are presented in Rial Omani, which is the Window's functional currency and also in US Dollars, for the convenience of the readers. The US Dollar amounts, which are presented in these financial statements have been translated from the Rial Omani amounts at an exchange rate of US Dollar 1 = RO 0.385. All financial information presented in Rial Omani and US Dollars has been rounded off to the nearest thousands.

A2.3 Use of Judgments and estimates

In the process of applying the Window's accounting policies, management uses judgments and makes estimates in determining the amounts recognized in the financial statements. These estimates and assumptions effect the amount of assets and liabilities and disclosure of contingent liabilities, as these estimates and interpretations effect revenues, expenses and allowances, as well as changes in fair value.

Estimates and underlying assumptions are reviewed on regular basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised and in any future periods affected. The most significant uses of judgments and estimates are as follows:

Impairment provisions against financing contracts with customers

The Window reviews its financing contracts at each reporting date to assess whether an impairment provision should be recorded in the financial statements. In particular, judgment by management is required in the estimation of the amount and timing of future cash flows when determining the level of provision required. Such estimates are based on assumptions about factors involving varying degrees of judgment and uncertainty and actual results may differ resulting in future changes to the provisions.

A2 BASIS OF PREPARATION (continued)

A2.3 Use of Judgments and estimates (continued)

Impairment provisions against financing contracts with customers (continued)

In addition to specific provisions against individually significant financing contracts, the Window also makes collective impairment provision against exposures which, although not specifically identified as requiring a specific provision, have a greater risk of default than when originally granted. This takes into consideration, factors such as any deterioration in country risk, industry, and technological obsolescence, as well as identified structural weaknesses or deterioration in cash flows.

Classification of investments

Management decides upon acquisition of an investment whether it should be classified as fair value through statement of income, fair value through equity or at amortised cost.

Liquidity

The Window manages its liquidity through consideration of the maturity profile of its assets and liabilities which is set out in the liquidity risk disclosures in note D2.2. This requires judgment when determining the maturity of assets and liabilities with no specific maturities.

A2.4 New standards, interpretations and amendments

These financial statements have been prepared using accounting policies, which are consistent with those used in the preparation of the annual financial statements for the year ended 31 December 2018.

There are no new standards issued by AAOIFI during the year which may impact the financial statements of the Window.

Standard issued and effective

New and amended standards and interpretations

In these financial statements, the Bank has applied IFRS 9 and IFRS 7R, effective for annual periods beginning on or after 1 January 2018, for the first time. The Bank has not adopted early any other standard, interpretation or amendment that has been issued but is not yet effective.

A2.4.a IFRS 9 Financial Instruments

IFRS 9 replaces IAS 39 for annual periods on or after 1 January 2018. The Bank elected, as a policy choice permitted under IFRS 9, to continue to apply hedge accounting in accordance with IAS 39.

The Bank has not restated comparative information for 2017 for financial instruments in the scope of IFRS 9. Therefore, the comparative information for 2017 is reported under IAS 39 and is not comparable to the information presented for 2018. Differences arising from the adoption of IFRS 9 have been recognised directly in retained earnings as of 1 January 2018 and are disclosed in Note A5.

(i) Changes to classification and measurement

To determine their classification and measurement category, IFRS 9 requires all financial assets, except equity instruments and derivatives, to be assessed based on a combination of the entity's business model for managing the assets and the instruments' contractual cash flow characteristics. The IAS 39 measurement categories of financial assets (fair value through profit or loss (FVPL), available for sale (AFS), held-to-maturity and amortised cost) have been replaced by:

- Debt instruments at amortised cost;
- Debt instruments at fair value through other comprehensive income (FVOCI), with gains or losses recycled to profit or loss on derecognition;
- Equity instruments at FVOCI, with no recycling of gains or losses to profit or loss on derecognition; or
- Financial assets FVPL.

The accounting for financial liabilities remains largely the same as it was under IAS 39, except for the treatment of gains or losses arising from an entity's own credit risk relating to liabilities designated at FVPL. Such movements are presented in OCI with no subsequent reclassification to the income statement.

A2 BASIS OF PREPARATION (continued)

A2.4 New standards, interpretations and amendments (continued)

Standard issued and effective (continued)

A2.4.a IFRS 9 Financial Instruments (continued)

Under IFRS 9, embedded derivatives are no longer separated from a host financial asset. Instead, financial assets are classified based on the business model and their contractual terms, as explained in Note A2.4.a (i). The accounting for derivatives embedded in financial liabilities and in non-financial host contracts has not changed.

The Window's classification of its financial assets and liabilities is explained in Notes A4.3.d. The quantitative impact of applying IFRS 9 as at 1 January 2018 is disclosed in Note A5.

(ii) Changes to the impairment calculation

The adoption of IFRS 9 has fundamentally changed the Bank's accounting for financing and advances loss impairments by replacing IAS 39's incurred loss approach with a forward-looking expected credit loss (ECL) approach. IFRS 9 requires the Bank to record an allowance for ECLs for all financing and advances and other debt financial assets not held at FVPL, together with financing and advances commitments and financial guarantee contracts. The allowance is based on the ECLs associated with the probability of default in the next twelve months unless there has been a significant increase in credit risk since origination. If the financial asset meets the definition of purchased or originated credit impaired (POCI), the allowance is based on the change in the ECLs over the life of the asset.

Details of the Window's impairment method are disclosed in Note A4.3.g. The quantitative impact of applying IFRS 9 as at 1 January 2018 is disclosed in Note A5.

A2.4.b IFRS 7R Financial Instruments Disclosures

To reflect the differences between IFRS 9 and IAS 39, IFRS 7 Financial Instruments: Disclosures was updated and the Bank has adopted it, together with IFRS 9, for the year beginning 1 January 2018. Changes include transition disclosures as shown in Note A5 and detailed qualitative and quantitative information about the ECL calculations such as the assumptions and inputs used are set out in Note A2.3.g.

Standard issued but not yet effective

A2.4.c IFRS 16 – Leases

The IASB issued IFRS 16 Leases (IFRS 16), which requires lessees to recognise assets and liabilities for most leases. The standard includes two recognition exemptions for lessees – leases of 'low-value' assets (e.g., personal computers) and short-term leases (i.e., leases with a lease term of 12 months or less). For lessors, there is little change to the existing accounting in IAS 17 Leases. The new standard will be effective for annual periods beginning on or after 1 January 2019. IFRS 16 also requires lessees and lessors to make more extensive disclosures than under IAS 17. The Window is still in the process of assessing the potential impact of IFRS 16 on these financial statements

A2.4.d FAS 28 Murabaha and Other Deferred Payment Sales

AAOIFI has issued FAS 28 Murabaha and Other Deferred Payment Sales in 2017. FAS 28 supersedes the earlier FAS No. 2 "Murabaha and Murabaha to the Purchase Orderer" and FAS No. 20 "Deferred Payment Sale". The objective of this standard is to prescribe the appropriate accounting and reporting principles for recognition, measurement and disclosures in relation to Murabaha and other deferred payment sales transactions for the sellers and buyers, for such transactions. This standard shall be effective for the financial periods beginning on or after 1 January 2019 with early adoption permitted.

The Window is currently evaluating the impact of this standard.

A2.4.e FAS 31 Investment Agency (Al-Wakala Bi Al-lstithmar)

AAOIFI has issued FAS 31 Investment Agency (Al-Wakala Bi Al-lstithmar) in 2018. The objective of this standard is to establish the principles of accounting and financial reporting for the investment agency (Al-Wakala Bi Al- Istithmar) instruments and the related assets and obligations from both the principal (investor) and the agent perspectives. This standard shall be effective for the financial periods beginning on or after 1 January 2020 with early adoption permitted.

The Window is currently evaluating the impact of this standard.

A2 BASIS OF PREPARATION (continued)

A2.4 New standards, interpretations and amendments (continued)

Standard issued but not yet effective (continued)

A2.4.f FAS 35 Risk Reserves

AAOIFI has issued FAS 35 "Risk Reserves" in 2018. This standard along with FAS 30 'Impairment, Credit losses and onerous commitments' supersede the earlier FAS 11 "Provisions and reserves".

The objective of this standard is to establish the principles of accounting and financial reporting for risk reserves established to mitigate various risks faced by stakeholders, mainly the profit and loss taking investors, of Islamic financial institutions (IFIs/ the institutions). This standard shall be effective for the financial periods beginning on or after 1 January 2021 with early adoption permitted only if the Group early adopts FAS 30 "Impairment, Credit losses and onerous commitments".

The Window is currently evaluating the impact of this standard.

A2.4.g FAS 30 Impairment, Credit losses and onerous commitments

In November 2017, the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) issued Financial Accounting Standard (FAS) 30 - Impairment, credit losses and onerous commitments, the standard supersedes the earlier FAS 11 "Provisions and Reserves" effective from the financial periods beginning on or after 1 January 2020, with early adoption permitted.

However, during the year 2017, the CBO had issued a circular BM 1149 dated 13 April 2017 governing implementation of IFRS 9 Financial Instruments (IFRS 9) for all the banks, which also apply to Islamic banks/windows subject to any specific instructions by the Central Bank for Islamic Banking entities on IFRS 9 if, as and when instructions are issued.

As mentioned in note A2.4.a, the Window adopted IFRS 9 on 1 January 2018 and did not restate the comparative information in accordance with relevant requirements of IFRS 9. For more details, please refer to note A2.4.a.

A3 SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies adopted in the preparation of the financial statements are set out below:

A3.1 Cash and cash equivalents

Cash and cash equivalents comprise cash on hand and balances with central bank and placements with banks and financial institutions that mature within three months, less borrowings with banks and financial institutions accounts that mature within three months and restricted balances.

A3.2 Foreign currency transactions

Transactions in foreign currencies are translated into functional currency at the spot exchange rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated into the functional currency at the spot exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for the effective profit and payments during the period, and the amortised cost in the foreign currency translated at the spot exchange rate at the end of the period. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

A3.3 Financing assets

Financing assets comprise Shari'a compliant financing provided by the Window with fixed or determinable payments. These include financing provided through Murabaha, Mudaraba, Musharaka, Musawama, Ijarah, Istisna and other modes of Islamic financing. Financing assets are stated at their amortised cost less impairment allowances (if any).

Murabaha

Murabaha receivables are sales on deferred terms. The Window arranges a Murabaha transaction by buying a commodity (which represents the object of the Murabaha) and selling it to the Murabeh (a beneficiary) at a margin of profit over cost. The sales price (cost plus the profit margin) is repaid in instalments by the Murabeh over the agreed period. Murabaha receivables are stated net of deferred profits and impairment allowance (if any). Any promise made by potential Murabeh is considered obligatory.

A3 SIGNIFICANT ACCOUNTING POLICIES (continued)

A3.3 Financing assets (continued)

Mudaraba

Mudaraba is stated at the fair value of consideration given less any impairment.

Mudaraba is a form of partnership between work and capital in which the Window contributes capital. Mudaraba capital provided by the Window at inception in kind (if other than cash) is measured at the fair value of the assets. If the valuation of assets results in difference between fair value and book value, such difference is recognised as profit or loss to the Window.

In case mudaraba capital is lost or damaged prior to the inception of work without misconduct or negligence on the part of mudarib, then such losses are deducted from mudaraba capital and are treated as loss to the Window. In case of termination or liquidation, unpaid portion by mudarib is recognised as receivable due from mudarib.

Musharaka

Musharaka contracts represents a partnership between the Window and a customer whereby each party contributes to the capital in equal or varying proportions to establish a new project or share in an existing one, and whereby each of the parties becomes an owner of the capital on a permanent or declining basis and shall share profits or losses. These are stated at the fair value of consideration given less any amounts written off and provision for impairment, if any. In Diminishing Musharaka based transactions, Window enters into a Musharaka based on Shirkat-ul-milk for financing an agreed share of fixed asset (e.g. house, land, plant or machinery) with its customers and enters into period profit payment agreement for the utilisation of Window’s Musharaka share by the customer.

Ijarah muntahia bittamleek

These are initially recorded at cost including initial direct costs. Ijarah muntahia bittamleek is a lease whereby the legal title of the leased asset passes to the lessee at the end of the ijarah (lease term), provided that all ijarah installments are settled.

Depreciation is charged on Ijarah muntahia bittamleek assets at rates calculated to write off the cost of each asset over its lease term.

Ijarah income receivables represent outstanding rentals at the end of the year less any provision for doubtful amount. The ijarah income receivable is classified under other asset.

Istisna followed by Ijarah muntahia bittamleek

Istisna followed by Ijarah muntahia bittamleek is construction finance product in which property is developed under istisna` contract between customer and the Bank. Banks develops the property and then after completion of construction the property is leased to customer under Ijarah muntahia bittamleek contract. During construction customer pays the advance rentals.

Salam

In a Salam contract a buyer pays in advance for a specified quantity and quality of a commodity, deliverable on a specific date, at an agreed spot price. Salam is particularly applicable to seasonal agricultural purchases and can be used as a means of financing production. The price is paid at the time of the contract but the delivery would take place at a future date which enables an entrepreneur to sell his output to the Window at a price determined in advance. However, at the time of sale all specifications, quality and quantity of the commodity must be determined to avoid any ambiguity which could become a cause of dispute. Furthermore, date and time of delivery must also be agreed upon but can be changed with mutual consent of the parties. Salam contracts are recognised on the date at which they are originated and are carried at their cost less impairment allowances, if any.

A3 SIGNIFICANT ACCOUNTING POLICIES (continued)

A3.3 Financing assets (continued)

Diminishing Musharakah

In Diminishing Musharakah financing, the Bank enters into Musharakah based on Shirkat-ul-milk for financing an agreed share of fixed asset (e.g. house, land, plant or machinery) with its customers and enters into period profit payment agreement for the utilisation of the Bank's Musharakah share by the customer.

A3.4 Financial instruments – initial recognition

A3.4.a Date of recognition

Financial assets and liabilities, with the exception of financing assets to customers and balances due to customers, are initially recognised on the trade date, i.e., the date that the Bank becomes a party to the contractual provisions of the instrument. This includes regular way trades: purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place. Loans and advances to customers are recognised when funds are transferred to the customers' accounts. The Bank recognises balances due to customers when funds are transferred to the Bank.

A3.4.b Initial measurement of financial instruments

The classification of financial instruments at initial recognition depends on their contractual terms and the business model for managing the instruments. Financial instruments are initially measured at their fair value (except in the case of financial assets and financial liabilities recorded at FVPL, transaction costs are added to, or subtracted from, this amount. Trade receivables are measured at the transaction price. When the fair value of financial instruments at initial recognition differs from the transaction price, the Bank accounts for the Day 1 profit or loss, as described below.

A3.4.c Day 1 profit or loss

When the transaction price of the instrument differs from the fair value at origination and the fair value is based on a valuation technique using only inputs observable in market transactions, the Bank recognises the difference between the transaction price and fair value in net trading income. In those cases where fair value is based on models for which some of the inputs are not observable, the difference between the transaction price and the fair value is deferred and is only recognised in profit or loss when the inputs become observable, or when the instrument is derecognised.

A3.4.d Measurement categories of financial assets and liabilities

From 1 January 2018, the Bank classifies all of its financial assets based on the business model for managing the assets and the asset's contractual terms, measured at either:

- Amortised cost, as explained in Note A3.4.d(i);
- FVOCI, as explained in Notes A3.4.d (iv) and A3.4.d(v); or
- FVPL, as explained in Note A3.4.d(vii)

The Bank classifies and measures its derivative and trading portfolio at FVTPL The Bank may designate financial instruments at FVTPL, if so doing eliminates or significantly reduces measurement or recognition inconsistencies.

(i) Due from banks, Loans and advances to customers, financial investments at amortised cost

Before 1 January 2018, Due from bank and Loans and advances to customers, included non–derivative financial assets with fixed or determinable payments that were not quoted in an active market, other than those:

- That the Bank intended to sell immediately or in the near term;
- That the Bank, upon initial recognition, designated as at FVPL or as available-for-sale; or

- For which the Bank may not recover substantially all of its initial investment, other than because of credit deterioration, which were designated as available-for-sale.

A3 SIGNIFICANT ACCOUNTING POLICIES (continued)

A3.4 Financial instruments – initial recognition (continued)

A3.4.d Measurement categories of financial assets and liabilities (continued)

From 1 January 2018, the Bank only measures Due from banks, Loans and advances to customers and other financial investments at amortised cost if both of the following conditions are met:

- The financial asset is held within a business model with the objective to hold financial assets in order to collect contractual cash flows; and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest (SPPI) on the principal amount outstanding.

The details of these conditions are outlined below.

- Business model assessment

The Bank determines its business model at the level that best reflects how it manages groups of financial assets to achieve its business objective. The Bank's business model is not assessed on an instrument-by-instrument basis, but at a higher level of aggregated portfolios and is based on observable factors such as:

- How the performance of the business model and the financial assets held within that business model are evaluated and reported to the entity's key management personnel;
- The risks that affect the performance of the business model (and the financial assets held within that business model) and, in particular, the way those risks are managed;
- How managers of the business are compensated (for example, whether the compensation is based on the fair value of the assets managed or on the contractual cash flows collected); and
- The expected frequency, value and timing of sales are also important aspects of the Bank's assessment.

The business model assessment is based on reasonably expected scenarios without taking 'worst case' or 'stress case' scenarios into account. If cash flows after initial recognition are realised in a way that is different from the Bank's original expectations, the Bank does not change the classification of the remaining financial assets held in that business model, but incorporates such information when assessing newly originated or newly purchased financial assets going forward.

- The SPPI test

As a second step of its classification process the Bank assesses the contractual terms of financial assets to identify whether they meet the SPPI test. 'Principal' for the purpose of this test is defined as the fair value of the financial asset at initial recognition and may change over the life of the financial asset (for example, if there are repayments of principal or amortisation of the premium/discount).

The most significant elements of interest within a lending arrangement are typically the consideration for the time value of money and credit risk. To make the SPPI assessment, the Bank applies judgement and considers relevant factors such as the currency in which the financial asset is denominated, and the period for which the interest rate is set.

In contrast, contractual terms that introduce a more than the minimum exposure to risks or volatility in the contractual cash flows that are unrelated to a basic lending arrangement do not give rise to contractual cash flows that are solely payments of principal and interest on the amount outstanding. In such cases, the financial asset is required to be measured at FVTPL.

(ii) Derivatives recorded at fair value through profit or loss

A derivative is a financial instrument or other contract with all three of the following characteristics:

- Its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable, provided that, in the case of a non-financial variable, it is not specific to a party to the contract (i.e., the 'underlying').

A3 SIGNIFICANT ACCOUNTING POLICIES (continued)

A3.4 Financial instruments – initial recognition (continued)

A3.4.d Measurement categories of financial assets and liabilities (continued)

(ii) Derivatives recorded at fair value through profit or loss (continued)

- It requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts expected to have a similar response to changes in market factors.
- It is settled at a future date.

The Bank enters into derivative transactions with various counterparties. These include interest rate swaps, futures, cross-currency swaps, forward foreign exchange contracts and options on interest rates, foreign currencies. Derivatives are recorded at fair value and carried as assets when their fair value is positive and as liabilities when their fair value is negative. The notional amount and fair value of such derivatives are disclosed separately in Note B17. Changes in the fair value of derivatives are included in net trading income unless hedge accounting is applied. Hedge accounting disclosures are provided in Note A4.4.m.

(iii) Embedded derivatives

An embedded derivative is a component of a hybrid instrument that also includes a non-derivative host contract with the effect that some of the cash flows of the combined instrument vary in a way similar to a stand-alone derivative. An embedded derivative causes some or all of the cash flows that otherwise would be required by the contract to be modified according to a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable, provided that, in the case of a non-financial variable, it is not specific to a party to the contract. A derivative that is attached to a financial instrument, but is contractually transferable independently of that instrument, or has a different counterparty from that instrument, is not an embedded derivative, but a separate financial instrument. Under IAS 39, derivatives embedded in financial assets, liabilities and non-financial host contacts, were treated as separate derivatives and recorded at fair value if they met the definition of a derivative (as defined above), their economic characteristics and risks were not closely related to those of the host contract, and the host contract was not itself held for trading or designated at FVPL. The embedded derivatives separated from the host were carried at fair value in the trading portfolio with changes in fair value recognised in the income statement.

From 1 January 2018, with the introduction of IFRS 9, the Bank continues to accounts in this way for derivatives embedded in financial liabilities and non-financial host contracts. Financial assets are, however, classified based on the business model and SPPI assessments as outlined in Note A3.4.d (i).

(iv) Financial assets or financial liabilities held for trading

The Bank classifies financial assets or financial liabilities as held for trading when they have been purchased or issued primarily for short-term profit making through trading activities or form part of a portfolio of financial instruments that are managed together, for which there is evidence of a recent pattern of short-term profit taking. Held-for-trading assets and liabilities are recorded and measured in the statement of financial position at fair value. Changes in fair value are recognised in net trading income. Interest and dividend income or expense is recorded in net trading income according to the terms of the contract, or when the right to payment has been established.

Included in this classification are debt securities, equities, short positions and customer loans that have been acquired principally for the purpose of selling or repurchasing in the near term.

(v) Debt instruments at FVOCI (Policy applicable from 1 January 2018)

The Bank applies the new category under IFRS 9 of debt instruments measured at FVOCI when both of the following conditions are met:

- The instrument is held within a business model, the objective of which is achieved by both collecting contractual cash flows and selling financial assets; and
- The contractual terms of the financial asset meet the SPPI test.

A3 SIGNIFICANT ACCOUNTING POLICIES (continued)

A3.4 Financial instruments – initial recognition (continued)

A3.4.d Measurement categories of financial assets and liabilities (continued)

(v) Debt instruments at FVOCI (Policy applicable from 1 January 2018) (continued)

These instruments largely comprise assets that had previously been classified as financial investments available for sale under IAS 39. FVOCI debt instruments are subsequently measured at fair value with gains and losses arising due to changes in fair value recognised in OCI. Interest income and foreign exchange gains and losses are recognised in profit or loss in the same manner as for financial assets measured at amortised cost as explained in Note A3.4.d(i). The ECL calculation for Debt instruments at FVOCI is explained in Note A3.4.g(iii) Where the Bank holds more than one investment in the same security, they are deemed to be disposed of on a first–in first–out basis. On derecognition, cumulative gains or losses previously recognised in OCI are reclassified from OCI to profit or loss.

(vi) Equity instruments at FVOCI (Policy applicable from 1 January 2018)

Upon initial recognition, the Bank occasionally elects to irrevocably classify some of its equity investments as equity instruments at FVOCI when they meet the definition of Equity under IAS 32 Financial Instruments: Presentation and are not held for trading. Such classification is determined on an instrument by instrument basis.

Gains and losses on these equity instruments are never recycled to profit. Dividends are recognised in profit or loss as other operating income when the right of the payment has been established, except when the Bank benefits from such proceeds as a recovery of part of the cost of the instrument, in which case, such gains are recorded in OCI. Equity instruments at FVOCI are not subject to an impairment assessment.

(vii) Financial assets and financial liabilities at fair value through profit or loss

Financial assets and financial liabilities in this category are those that are not held for trading and have been either designated by management upon initial recognition or are mandatorily required to be measured at fair value under IFRS 9. Management only designates an instrument at FVPL upon initial recognition when one of the following criteria is met. Such designation is determined on an instrument by instrument basis:

- The designation eliminates, or significantly reduces, the inconsistent treatment that would otherwise arise from measuring the assets or liabilities or recognising gains or losses on them on a different basis;
- The liabilities (and assets until 1 January 2018 under IAS 39) are part of a group of financial liabilities (or financial assets, or both under IAS 39), which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management or investment strategy; or
- The liabilities (and assets until 1 January 2018 under IAS 39) containing one or more embedded derivatives, unless they do not significantly modify the cash flows that would otherwise be required by the contract, or it is clear with little or no analysis when a similar instrument is first considered that separation of the embedded derivative(s) is prohibited

Financial assets and financial liabilities at FVTPL are recorded in the statement of financial position at fair value. Changes in fair value are recorded in profit and loss with the exception of movements in fair value of liabilities designated at FVPL due to changes in the Bank's own credit risk. Such changes in fair value are recorded in the Own credit reserve through OCI and do not get recycled to the profit or loss. Interest earned or incurred on instruments designated at FVPL is accrued in interest income or interest expense, respectively, using EIR, taking into account any discount/premium and qualifying transaction costs being an integral part of instrument. Interest earned on assets mandatorily required to be measured at FVPL is recorded using contractual interest rate. Dividend income from equity instruments measured at FVTPL is recorded in profit or loss as other operating income when the right to the payment has been established.

A3 SIGNIFICANT ACCOUNTING POLICIES (continued)

A3.4 Financial instruments – initial recognition (continued)

A3.4.d Measurement categories of financial assets and liabilities (continued)

(viii) Financial guarantees, letters of credit and undrawn loan commitments

The Bank issues financial guarantees, letters of credit and loan commitments.

Financial guarantees are initially recognised in the financial statements (within Provisions) at fair value, being the premium received. Subsequent to initial recognition, the Bank's liability under each guarantee is measured at the higher of the amount initially recognised less cumulative amortisation recognised in the income statement, and – under IAS 39 – the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee, or – under IFRS 9 – an ECL provision as set out in Note A3.4.g. The premium received is recognised in the income statement in Net fees and commission income on a straight line basis over the life of the guarantee.

Undrawn loan commitments and letters of credits are commitments under which, over the duration of the commitment, the Bank is required to provide a loan with pre-specified terms to the customer. Similar to financial guarantee contracts, under IAS 39, a provision was made if they were an onerous contract but, from 1 January 2018, these contracts are in the scope of the ECL requirements.

The nominal contractual value of financial guarantees, letters of credit and undrawn loan commitments, where the loan agreed to be provided is on market terms, are not recorded on in the statement of financial position.

The nominal values of these instruments together with the corresponding ECLs are disclosed in Note 11. The Bank occasionally issues loan commitments at below market interest rates drawdown. Such commitments are subsequently measured at the higher of the amount of the ECL allowance (as explained in Note A3.4.g) and the amount initially recognised less, when appropriate, the cumulative amount of income recognised.

(ix) Available for sale financial investments (Policy applicable before 1 January 2018)

Available for sale financial assets include equity and debt securities. Equity investments classified as available for sale are those which are neither classified as held for trading nor designated at fair value through profit or loss. Debt securities in this category are intended to be held for an indefinite period of time and may be sold in response to needs for liquidity or in response to changes in the market conditions.

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

After initial measurement, available for sale financial investments are subsequently measured at fair value.

Unrealised gains and losses are recognised directly in equity (other comprehensive income) in the change in fair value of available for sale financial assets. When the investment is disposed of, the cumulative gain or loss previously recognised in equity is recognised in the profit or loss in other operating income. Interest earned whilst holding available for sale financial investments is reported as interest income using the EIR. Dividends earned whilst holding available for sale financial investments are recognised in the profit or loss as other operating income when the right of the payment has been established. The losses arising from impairment of such investments are recognised in the profit or loss in impairment for available for sale financial assets and removed from the change in fair value of investments available for sale.

(x) Held to maturity financial investments (Policy applicable before 1 January 2018)

Held to maturity financial assets are non-derivative assets with fixed or determinable payments and fixed maturity that the Bank has the positive intent and ability to hold to maturity and which are not designated at fair value through profit or loss or available for sale.

These are initially recognised at fair value including direct and incremental transaction costs and measured subsequently at amortised cost, using the effective interest method.

A3 SIGNIFICANT ACCOUNTING POLICIES (continued)

A3.4 Financial instruments – initial recognition (continued)

A3.4.d Measurement categories of financial assets and liabilities (continued)

(x) Held to maturity financial investments (Policy applicable before 1 January 2018) (continued)

Interest on held to maturity investments is included in the statement of comprehensive income and reported as 'interest income'. In the case of impairment, the impairment loss is been reported as a deduction from the carrying value of the investment and recognised in the statement of comprehensive income as 'impairment for investments'.

A3.4.e Derecognition

(i) Financial assets

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

- The rights to receive cash flows from the asset have expired; or
- The Bank has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass–through' arrangement; and either:

  - The Bank has transferred substantially all the risks and rewards of the asset; or
  - The Bank has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset

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

(ii) Financial liabilities

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

A3.4.f Offsetting of financial assets and financial liabilities

Financial assets and financial liabilities are only offset and the net amount reported in the statement of financial position when there is a legally enforceable right to set off the recognised amounts and the Bank intends to either settle on a net basis or to realise the asset and settle the liability simultaneously. Income and expenses are presented on a net basis only when permitted by the accounting standards or for gains and losses arising from a group of similar transactions

A3.4.g Impairment of financial assets (Policy applicable from 1 January 2018)

(i) Overview of the ECL principles

The adoption of IFRS 9 has fundamentally changed the Bank's loan loss impairment method by replacing IAS 39's incurred loss approach with a forward-looking ECL approach. From 1 January 2018, the Bank has been recording the allowance for expected credit losses for all loans and other debt financial assets not held at FVPL, together with loan commitments and financial guarantee contracts, in this section all referred to as 'financial instruments'. Equity instruments are not subject to impairment under IFRS 9.

A3 SIGNIFICANT ACCOUNTING POLICIES (continued)

A3.4.g Impairment of financial assets (Policy applicable from 1 January 2018)

(i) Overview of the ECL principles

The ECL allowance is based on the credit losses expected to arise over the life of the asset (the lifetime expected credit loss or LTECL), unless there has been no significant increase in credit risk since origination, in which case, the allowance is based on the 12 months' expected credit loss (12mECL). The Bank's policies for determining if there has been a significant increase in credit risk.

The 12mECL is the portion of LTECLs that represent the ECLs that result from default events on a financial instrument that are possible within the 12 months after the reporting date. Both LTECLs and 12mECLs are calculated on either an individual basis or a collective basis, depending on the nature of the underlying portfolio of financial instruments.

The Bank has established a policy to perform an assessment, at the end of each reporting period, of whether a financial instrument's credit risk has increased significantly since initial recognition, by considering the change in the risk of default occurring over the remaining life of the financial instrument.

Based on the above process, the Bank groups its loans into Stage 1, Stage 2, Stage 3 and POCI, as described below:

- Stage 1: When loans are first recognised, the Bank recognises an allowance based on 12mECLs. Stage 1loans also include facilities where the credit risk has improved and the loan has been reclassified from Stage 2.
- Stage 2: When a loan has shown a significant increase in credit risk since origination, the Bank records an allowance for the LTECLs. Stage 2 loans also include facilities, where the credit risk has improved and the loan has been reclassified from Stage 3.
- Stage 3: Loans considered credit-impaired .The bank records an allowance for the LTECLs.

  For financial assets for which the Bank has no reasonable expectations of recovering either the entire outstanding amount, or a proportion thereof, the gross carrying amount of the financial asset is reduced. This is considered a (partial) derecognition of the financial asset.

(ii) The calculation of ECLs

The Bank calculates ECLs based on a four probability-weighted scenarios to measure the expected cash shortfalls, discounted at an approximation to the EIR. A cash shortfall is the difference between the cash flows that are due to an entity in accordance with the contract and the cash flows that the entity expects to receive.

The mechanics of the ECL calculations are outlined below and the key elements are, as follows:

- PD - The Probability of Default is an estimate of the likelihood of default over a given time horizon. A default may only happen at a certain time over the assessed period, if the facility has not been previously derecognised and is still in the portfolio.
- EAD - The Exposure at Default is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date, including repayments of principal and interest, whether scheduled by contract or otherwise, expected drawdowns on committed facilities, and accrued interest from missed payments.
- LGD - The Loss Given Default is an estimate of the loss arising in the case where a default occurs at a given time. It is based on the difference between the contractual cash flows due and those that the Bank would expect to receive, including from the realisation of any collateral. It is usually expressed as a percentage of the EAD.

When estimating the ECLs, the Bank considers four scenarios (a base case, an upside, a mild downside ('downside 1') and a more extreme downside ('downside 2')). Each of these is associated with different PDs, EADs and LGDs. When relevant, the assessment of multiple scenarios also incorporates how defaulted loans are expected to be recovered, including the probability that the loans will cure and the value of collateral or the amount that might be received for selling the asset.

With the exception of credit cards and other revolving facilities, the maximum period for which the credit losses are determined is the contractual life of a financial instrument unless the Bank has the legal right to call it earlier.

A3 SIGNIFICANT ACCOUNTING POLICIES (continued)

A3.4.g Impairment of financial assets (Policy applicable from 1 January 2018)

(ii) The calculation of ECLs (continued)

Impairment losses and releases are accounted for and disclosed separately from modification losses or gains that are accounted for as an adjustment of the financial asset's gross carrying value.

The mechanics of the ECL method are summarised below:

- Stage 1: The 12mECL is calculated as the portion of LTECLs that represent the ECLs that result from default events on a financial instrument that are possible within the 12 months after the reporting date. The Bank calculates the 12mECL allowance based on the expectation of a default occurring in the 12 months following the reporting date. These expected 12-month default probabilities are applied to a forecast EAD and multiplied by the expected LGD and discounted by an approximation to the original EIR. This calculation is made for each of the four scenarios, as explained above.
- Stage 2: When a loan has shown a significant increase in credit risk since origination, the Bank records an allowance for the LTECLs. The mechanics are similar to those explained above, including the use of multiple scenarios, but PDs and LGDs are estimated over the lifetime of the instrument. The expected cash shortfalls are discounted by an approximation to the original EIR.
- Stage 3: For loans considered credit-impaired, the Bank recognises the lifetime expected credit losses for these loans. The method is similar to that for Stage 2 assets, with the PD set at 100%.
- POCI: POCI assets are financial assets that are credit impaired on initial recognition. The Bank only recognises the cumulative changes in lifetime ECLs since initial recognition, based on a probability-weighting of the four scenarios, discounted by the credit adjusted EIR.
- Loan commitments and letters of credit: When estimating LTECLs for undrawn loan commitments, the Bank estimates the expected portion of the loan commitment that will be drawn down over its expected life. The ECL is then based on the present value of the expected shortfalls in cash flows if the loan is drawn down, based on a probability-weighting of the four scenarios. The expected cash shortfalls are discounted at an approximation to the expected EIR on the loan.
- Credit cards and revolving facilities that include both a loan and an undrawn commitment, ECLs are calculated and presented together with the loan. For loan commitments and letters of credit, the ECL is recognised within Provisions.
- Financial guarantee contracts: The Bank's liability under each guarantee is measured at the higher of the amount initially recognised less cumulative amortisation recognised in the income statement, and the ECL provision. For this purpose, the Bank estimates ECLs based on the present value of the expected payments to reimburse the holder for a credit loss that it incurs. The shortfalls are discounted by the risk-adjusted interest rate relevant to the exposure. The calculation is made using a probability-weighting of the four scenarios. The ECLs related to financial guarantee contracts are recognised within Provisions.

(iii) Debt instruments measured at fair value through OCI

The ECLs for debt instruments measured at FVOCI do not reduce the carrying amount of these financial assets in the statement of financial position, which remains at fair value. Instead, an amount equal to the allowance that would arise if the assets were measured at amortised cost is recognised in OCI as an accumulated impairment amount, with a corresponding charge to profit or loss. The accumulated loss recognised in OCI is recycled to the profit and loss upon derecognition of the assets.

(iv) Purchased or originated credit impaired financial assets (POCI)

For POCI financial assets, the Bank only recognises the cumulative changes in LTECL since initial recognition in the loss allowance.

(v) Credit cards and other revolving facilities

The Bank's product offering includes a variety of corporate and retail overdraft and credit cards facilities, in which the Bank has the right to cancel and/or reduce the facilities with one day's notice. The Bank does not limit its exposure to credit losses to the contractual notice period, but, instead calculates ECL over a period that reflects the Bank's expectations of the customer behaviour, its likelihood of default and the Bank's future risk mitigation procedures, which could include reducing or cancelling the facilities.

A3 SIGNIFICANT ACCOUNTING POLICIES (continued)

A3.4.g Impairment of financial assets (Policy applicable from 1 January 2018)

(v) Credit cards and other revolving facilities (continued)

The ongoing assessment of whether a significant increase in credit risk has occurred for revolving facilities is similar to other lending products. This is based on shifts in the customer's internal credit grade, but greater emphasis is also given to qualitative factors such as changes in usage.

The interest rate used to discount the ECLs for credit cards is based on the average effective interest rate that is expected to be charged over the expected period of exposure to the facilities. This estimation takes into account that many facilities are repaid in full each month and are consequently charged no interest.

(vi) Forward looking information

In its ECL models, the Bank relies on a broad range of forward looking information as economic inputs, such as:

- GDP growth
- Unemployment rates
- Central Bank base rates
- House price indices

The inputs and models used for calculating ECLs may not always capture all characteristics of the market at the date of the financial statements. To reflect this, qualitative adjustments or overlays are occasionally made as temporary adjustments when such differences are significantly material.

(vii) Collateral valuation

To mitigate its credit risks on financial assets, the Bank seeks to use collateral, where possible. The collateral comes in various forms, such as cash, securities, letters of credit/guarantees, real estate, receivables, inventories, other non-financial assets and credit enhancements such as netting agreements. The Bank's accounting policy for collateral assigned to it through its lending arrangements under IFRS 9 is the same as it was under IAS 39. Collateral, unless repossessed, is not recorded on the Bank's statement of financial position. However, the fair value of collateral affects the calculation of ECLs. It is generally assessed, at a minimum, at inception and re-assessed periodically based on the type of asset, for example, cash or securities relating to margining requirements, is valued daily.

To the extent possible, the Bank uses active market data for valuing financial assets held as collateral. Other financial assets which do not have readily determinable market values are valued using models. Non-financial collateral, such as real estate, is valued by certified third party valuers.

(viii) Write-offs

The Bank's accounting policy under IFRS 9 remains the same as it was under IAS 39. Financial assets are written off either partially or in their entirety only when the Bank has stopped pursuing the recovery. If the amount to be written off is greater than the accumulated loss allowance, the difference is first treated as an addition to the allowance that is then applied against the gross carrying amount. Any subsequent recoveries are credited to credit loss expense.

(ix) Forborne and modified loans

The Bank sometimes makes concessions or modifications to the original terms of loans as a response to the borrower's financial difficulties, rather than taking possession or to otherwise enforce collection of collateral. The Bank considers a loan forborne when such concessions or modifications are provided as a result of the borrower's present or expected financial difficulties and the Bank would not have agreed to them if the borrower had been financially healthy. Indicators of financial difficulties include defaults on covenants or significant concerns raised by the Credit Risk Department. Forbearance may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, any impairment is measured using the original EIR as calculated before the modification of terms. It is the Bank's policy to monitor forborne loans to help ensure that future payments continue to be likely to occur.

A3 SIGNIFICANT ACCOUNTING POLICIES (continued)

A3.4.g Impairment of financial assets (Policy applicable from 1 January 2018)

(ix) Forborne and modified loans (continued)

Derecognition decisions and classification between Stage 2 and Stage 3 are determined on a case-by-case basis. If these procedures identify a loss in relation to a loan, it is disclosed and managed as an impaired Stage 3 forborne asset until it is collected or written off. From 1 January 2018, when the loan has been renegotiated or modified but not derecognised, the Bank also reassesses whether there has been a significant increase in credit risk. The Bank also considers whether the assets should be classified as Stage 3. Once an asset has been classified as forborne, it will remain forborne for a minimum 12-month probation period. In order for the loan to be reclassified out of the forborne category, the customer has to meet all of the following criteria:

- All of its facilities has to be considered performing
- The probation period of two years has passed from the date the forborne contract was considered performing
- Regular payments of more than an insignificant amount of principal or interest have been made during at least half of the probation period
- The customer does not have any contract that is more than 30 days past due.

The Bank assesses at each reporting date whether there is objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is impaired and an impairment loss is 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 as well as considering the guidelines issued by the Central Bank of Oman:

- significant financial difficulty of the issuer or obligor;
- a breach of contract, such as a default or delinquency in interest or principal payments;
- 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;
- it becoming probable that the borrower will enter bankruptcy or other financial reorganisation;
- the disappearance of an active market for that financial asset because of financial difficulties; or
- 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.

(x) Assets carried at amortised cost

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 or held to maturity investments carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the statement of comprehensive income. If a loan or held to maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract.

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.

A3 SIGNIFICANT ACCOUNTING POLICIES (continued)

A3.4.g Impairment of financial assets (Policy applicable from 1 January 2018)

(x) Assets carried at amortised cost (continued)

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the group and historical loss experience for assets with credit risk characteristics similar to those in the group.

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 uncollectible, it is written off against the related allowance 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.

If in a subsequent period, the amount of impairment loss decreases and decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the statement of comprehensive income. Also refer to note B3 for loans, advances and financing.

(xi) Assets classified as available for sale

The Bank assesses at the end of each reporting period whether there is objective evidence that a financial asset or a group of financial assets is impaired. For debt securities, the Bank uses the criteria referred to at (x) above. 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 evidence that 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 profit or loss. Impairment losses on equity instruments recognised in the profit or loss are not reversed through statement of profit or loss.

A3.4.h Amortised cost measurement

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest rate of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

A3.4.i Fair value measurement

A number of the Bank's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on a number of accounting policies and methods. Where applicable, information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability, or
- In the absence of a principal market, in the most advantageous market for the asset or liability

The principal or the most advantageous market must be accessible to the Bank. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Bank uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

A3 SIGNIFICANT ACCOUNTING POLICIES (continued)

A3.4.i Fair value measurement (continued)

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1 — Quoted (unadjusted) market prices in active markets for identical assets or liabilities
- Level 2 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable
- Level 3 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Bank determines whether transfers have occurred between Levels in the hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

At each reporting date, the Bank analyses the movements in the values of assets and liabilities which are required to be re-measured or re-assessed as per the Bank's accounting policies. For this analysis, the Bank verifies the major inputs applied in the latest valuation by agreeing the information in the Valuation computation to contracts and other relevant documents.

The Bank also compares the changes in the fair value of each asset and liability with relevant external sources to determine whether the change is reasonable.

For the purpose of fair value disclosures, the Bank has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy as explained above.

A3.4.j Cash and cash equivalents

Cash and cash equivalents consist of cash in hand, unrestricted balances held with central banks and highly liquid financial assets with original maturities of up to three months, which are subject to insignificant risk of changes in their fair value, and are used by the Bank in management of its short term commitments. Cash and cash equivalents are carried at amortised cost in the statement of financial position.

A3.4.k Acceptances

Acceptances are disclosed on the statement of financial position under other assets with corresponding liability disclosed under other liabilities. Therefore, there is no off-balance sheet commitment for acceptances.

A3.4.l Derivatives held for risk management purposes

Derivatives held for risk management purposes include all derivative assets and liabilities that are not classified as trading assets or trading liabilities. Derivatives held for risk management purposes are measured at fair value in the statement of financial position. The treatment of changes in their fair value depends on their classification into the following categories:

(i) Cash flow hedge

When a derivative is designated as a hedge of the change in fair value of a recognised asset or liability or a firm commitment, changes in the fair value of the derivative are recognised immediately in statement of comprehensive income together with changes in the fair value of the hedged item that are attributable to the hedged risk.

If the derivative expires or is sold, terminated, or exercised, no longer meets the criteria for fair value hedge accounting, or the designation is revoked, hedge accounting is discontinued. Any adjustment up to that point, to a hedged item for which the effective interest method is used, is amortised to profit or loss as part of the recalculated effective interest rate of the item over its remaining life.

A3 SIGNIFICANT ACCOUNTING POLICIES (continued)

A3.4.l Derivatives held for risk management purposes (continued)

(ii) Cash flow hedge

When a derivative is designated as the hedging instrument in a hedge of the variability in cash flows attributable to a particular risk associated with a recognised asset or a liability or a highly probable forecast transaction that could affect profit or loss, the effective portion of changes in the fair value of the derivative is recognised in other comprehensive income in hedging reserve. The amount recognised in

other comprehensive income is reclassified to profit or loss as a reclassification adjustment in the same period as the hedged cash flows affect profit or loss, and in the same line item in the statement of comprehensive income. Any ineffective portion of changes in the fair value of the derivative is recognised immediately in profit or loss.

If the hedging derivative expires or is sold, terminated, or exercised, or the hedge no longer meets the criteria for cash flow hedge accounting, or the hedge designation is revoked, then the hedge accounting is discontinued prospectively. In a discontinued hedge of a forecast transaction the cumulative amount recognised in other comprehensive income from the period when the hedge was effective is reclassified from the equity to statement of comprehensive income as a reclassification adjustment when the forecast transaction occurs and affects profit or loss. If the forecast transaction is no longer expected to occur, then the balance in other comprehensive income is reclassified immediately to profit or loss as a reclassification adjustment.

(iii) Other non-trading derivative

When a derivative is not held for trading, and is not designated in a qualifying hedge relationship, all changes in its fair value are recognised immediately in statement of comprehensive income.

A3.5 Property, equipment and fixtures

Items of property, equipment and fixtures are measured at historical cost less accumulated depreciation and impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the asset. Depreciation is provided on a straight-line basis over the estimated useful lives of property, equipment and fixtures, except freehold land. The estimated useful lives for the current period are as follows:

	Years
Motor vehicles	5
Furniture and fixtures	6-7
Office equipment	6-7
Computer software	10

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

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised within 'other operating income' in the income statement.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Window and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

A3.6 Taxation

The tax return of the Bank is filed at head office level and the Window is not required to file a separate return on the activities of the Islamic Banking operations. During the year head office has started to allocate tax at flat rate of 15% of the Window's profit. Deferred tax assets and liabilities are recognised only at head office level.

A3 SIGNIFICANT ACCOUNTING POLICIES (continued)

A3.7 Employee benefits

End of service benefits
End of service indemnity for Omani employees are contributed in accordance with the terms of the Social Securities Law of 1991.

Provision for end of service indemnity for non-Omani employees has been made in accordance with the terms of the Oman Labour Law 2003 and its amendments and is based on current remuneration rates and cumulative years of service at the statement of financial position date. Employees' entitlements to annual leave and leave passage are recognised when they accrue to the employees up to the reporting date. These accruals are included in current liabilities, while that relating to end of service benefits is disclosed as a non-current liability.

Contributions to a defined contribution retirement plan for Omani employees in accordance with the Omani Social Insurance Law of 1991 are recognised as an expense in the statement of comprehensive income as incurred.

Short term benefits
Short term benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.
A provision is recognised for the amount expected to be paid if the Window has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

A3.8 Customer current accounts

Balances in current accounts are recognised when received by the Window. The transactions are measured as the amount received by the Window at the time of contracting. At the end of the reporting period, these accounts are measured at amortised cost.

A3.9 Equity of unrestricted investment account holders

The Window charges a management fee (Mudarib fee) to the unrestricted investment account holders. Of the total income from investments of funds, the income attributable to the unrestricted investment account holders is allocated to them after setting aside provisions, reserves (profit equalisation reserve and investment risk reserve), if any, and deducting the Window's share of income as a Mudarib. The allocation of income is determined by the management of the Window within the allowed profit sharing limits as per the terms and conditions of the unrestricted investment accounts.

A3.10 Due to and due from banks and Wakala Deposits

Due to and due from banks and financial institutions and customers comprise of wakala payables and receivables. Wakala payables and receivables are initially recognised at cost, being the fair value of consideration exchanged. Subsequently, they are carried at amortised cost less amounts repaid.

A3.11 Revenue recognition

Murabaha

Profit on Murabaha is recognised on an accrual basis. Profit on Murabaha transactions for the period from the date of disbursement to the date of culmination of Murabaha.

Mudaraba

Income on Mudaraba financing is recognised when the right to receive payment is established or on distribution by the Mudarib. Losses on the other hand are charged to the income statement on declaration by the Mudarib.

Musharaka

Income on musharaka is recognised when the right to receive payment is established or on distribution. In case of losses in musharaka, the Window's share of loss is recognised to the extent that such losses are being deducted from its share of the musharaka capital.

A3 SIGNIFICANT ACCOUNTING POLICIES (continued)

A3.11 Revenue recognition (continued)

Diminishing Musharakah

Profit on Diminishing Musharakah financings is recognised on an accrual basis.

Profit on sukuks

Profit on Sukuks is recognized on an accrual basis. Where Sukuks are purchased at a premium or discount and are classified at amortised cost, those premiums / discounts are amortised over the remaining maturity, using the effective profit rate method.

Ijarah

Ijarah rental income is recognised over the term of the lease on accrual basis and is stated net of depreciation and impairment. Income related to non performing ijarah muntahia bittamleek accounts and ijarah installments that are above 90 days is excluded from the statement of income.

Istisna followed by Ijarah muntahia bittamleek

Income for Istisna followed by Ijarah muntahia bittamleek is booked on receipt of the rentals.

Fees and commission income

Fees and commission income that are integral to the effective profit rate of a financial asset carried at amortised cost are included in the measurement of the effective profit rate of the financial asset. Other fees and commission income, including account servicing fees, sales commission, management, arrangement and syndication fees, are recognised as the related services are performed.

Window's share of income from equity of investment accountholders (as Rabalmal and Mudarib)

Income is allocated proportionately between equity of investment accountholders and shareholders on the basis of their respective investment in the pool before allocation of the Mudarib fees. The Window’s share as a Mudarib for managing the equity of investment accountholders is accrued based on the terms and conditions of the related Mudaraba agreements.

Salam

Income from salam is determined by using the percentage of completion method.

Dividend income

Dividend income is recognised when the right to receive the dividend is established.

Profit on amounts due from banks and financial institutions

Profit on amounts due from banks and financial institutions is recognised on a time apportioned basis over the period of the contract based on the principal amounts outstanding and the profit agreed with clients.

A3.12 Expense recognition

Return on equity of investment accountholders is calculated based on the income generated from joint investment accounts after deducting the expenses related to investment pool i.e. "mudarib expenses". Mudarib expenses include all expenses incurred by the Window, but excluding staff costs and other administrative expenses. The Window's "mudarib profit" is deducted from the investors' share of income before distributing such income.

A3 SIGNIFICANT ACCOUNTING POLICIES (continued)

A3.13 Earnings or expenditures prohibited by Sharia

The Window records these amounts in a separate account in the other payables and is not included in the Window’s revenues; these amounts are distributed to charities according to the Sharia Supervisory Board directions.

A3.14 Contingent liabilities

Contingent liabilities include guarantees, letter of credit, the Window’s obligations with respect to unilateral promise to buy/sell currencies and others. Contingent liabilities are not recognized in the statement of financial position but are disclosed in the notes to the financial statements, unless they are remote.

A3.15 Shari'a supervisory board

The Window's business activities are subject to the supervision of a Shari'a supervisory board consisting of members appointed by the general assembly of shareholders.

A3.16 Offsetting

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Bank has a legal right to set off the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously. The legally enforceable rights must not be contingent on future events and must be enforceable in the normal course of business and in the event of default, insolvency or bankruptcy of the Window and the counter party.

A3.17 Zakah

In accordance with the article of association Zakah is payable by individual shareholders of the Window and Zakah on unrestricted investment and other accounts is the responsibility of investment accountholders.

A3.18 Provisions

A provision is recognised if, as a result of a past event, the Window has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are equivalent to the amortised value of the future liabilities which is determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risk specific to the liability.

A3.19 Joint and self-financed

Assets that are jointly financed by the Window and the equity of investment accountholders are disclosed as "jointly financed" in the financial statements and assets that are financed solely by the Window are classified under "self financed".

A3.20 Profit equalisation reserve

Profit equalisation reserve, this is the amount appropriated out of Mudaraba income before allocating the Window’s share as investment manager (Mudarib), in order to maintain a certain level of return on investment for unrestricted investment accountholders and increase owners’ equity.

A3.21 Investment risk reserve

Investment risk reserve is the amount appropriated out of profit share of the unrestricted investment accountholders after allocating the Mudarib share, in order to cushion the effects of the risk of future investment losses. The terms and conditions whereby investment risk reserve can be set aside and utilised are determined and approved by the Shari’a Supervisory Board of the Window.

A3 SIGNIFICANT ACCOUNTING POLICIES (continued)

A3.22 Impairment reserve

The CBO has issued guidelines relating to the creation of impairment reserve, which is as set out below:

- Should the existing loan loss impairment computed in accordance with the requirements of IAS 39 and CBO guidelines be higher than the impairment allowance computed under IFRS 9, the related difference (net of tax) be transferred to a loan loss impairment reserve from retained earnings as of 1 January 2018.
- In the subsequent years, where the allowance for loan loss impairment computed in accordance with CBO requirements is higher than the allowance for loan loss impairment loss computed under IFRS 9, the difference (net of tax) should be transferred to the aforementioned loan loss impairment reserve from retained earnings.

The Window, as a policy decision, decided to review this position on a quarterly basis.

The related impairment reserve will not be available for dividend distribution or for inclusion in the regulatory capital. Any subsequent utilisation of the impairment reserve would require prior approval of the CBO.

A4 Critical accounting estimates and judgements

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and reported amounts of assets, liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. The resulting accounting estimates will, by definition, seldom equal the related actual results.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods. The Bank's significant accounting estimates are on:

A4.1 Impairment losses on loans and advances

The measurement of impairment losses both under IFRS 9 and IAS 39 across all categories of financial assets requires judgement, in particular, the estimation of the amount and timing of future cash flows and collateral values when determining impairment losses and the assessment of a significant increase in credit risk. These estimates are driven by a number of factors, changes in which can result in different levels of allowances. The Bank's ECL calculations are outputs of complex models with a number of underlying assumptions regarding the choice of variable inputs and their interdependencies. Elements of the ECL models that are considered accounting judgements and estimates include:

- The Bank's internal credit grading model, which assigns PDs to the individual grades;
- The Bank's criteria for assessing if there has been a significant increase in credit risk and so allowances for financial assets should be measured on a LTECL basis and the qualitative assessment;
- The segmentation of financial assets when their ECL is assessed on a collective basis;
- Development of ECL models, including the various formulas and the choice of inputs;
- Determination of associations between macroeconomic scenarios and economic inputs, such as unemployment levels and collateral values, and the effect on PDs, EADs and LGDs; and
- Selection of forward-looking macroeconomic scenarios and their probability weightings, to derive the economic inputs into the ECL models.

A4.2 Fair value estimation of unquoted securities

In cases where the underlying assets are fair valued such as private equity funds, management uses net assets value. Management believes that net assets values of these investments are representative of their fair values as the majority of the underlying assets are fair valued and the reported net assets of those entities takes into account the updated fair values changes.

A4.3 Fee and commission income

The recognition of fee and commission income depends on the purpose for which fees are assessed and the basis of accounting for any associated financial instrument. Management applies certain assumptions and judgements to determine the fees that are an integral part of the effective interest rate of a financial instrument, fees that are earned as services are provided, and fees that are earned on the execution of a significant act.

A5 Transition disclosures

The following pages set out the impact of adopting IFRS 9 on the statement of financial position, and retained earnings including the effect of replacing IAS 39's incurred credit loss model with IFRS 9's ECLs.

(i) The impact of transition to IFRS 9 on reserves and retained earnings is as follows:

	Retained earnings RO'000
Closing balance under IAS 39 as of 31 December 2017	**897**
Impact on reclassification and remeasurement:	**-**
Impact on recognition of Expected credit losses:	
Due from banks and financial institutions	**(5)**
Financing advances and other receivables at amortised cost, including commitments and financial guarantees	**(45)**
Debt securities at amortised cost	**(24)**
Adjusted opening balance under IFRS 9 on date of initial application of 1 January 2018	**823**

(ii) The Window performed a detailed analysis of its business models for managing financial assets as well as analysing their cash flow characteristics. The below table reconciles the original measurement categories and carrying amounts of financial assets in accordance with IAS 39 and the new measurement categories under IFRS 9 as at 31 December 2017.

	Original classification under IAS 39	New classification under IFRS 9	Original carrying amount RO'000	Re-measure ment RO'000	New carrying amount RO'000
Financial assets					
Cash and balances with central bank	AC	AC	**15,222**	**-**	**15,222**
Due from banks and financial institutions	AC	AC	**7,982**	**(5)**	**7,977**
Financings and advances	AC	AC	**144,922**	**(38)**	**144,884**
Investment securities – debt	HTM	AC	**10,476**	**(11)**	**10,465**
Investment securities – debt	HFT	FVTPL	**5,328**	**(13)**	**5,315**
Other assets	AC	AC	**1,713**	**-**	**1,713**
Off-balance sheet exposures					
Financing and advance commitments and financial guarantees	NA	NA	**-**	**(7)**	**(7)**
Net Impact			**185,643**	**(74)**	**185,569**

*ECL provision for financing and advance commitments and financial guarantees has been recognised under 'other liabilities'.

HFT – Held for trading; FVTPL – Fair value through profit and loss.

B 1 Cash and balances with Central Bank

	2018 RO'000	2017 RO'000
Balances with CBO:		
- current account	**2,155**	9,503
- cash reserve	**5,306**	4,667
Cash	**1,276**	1,052
	8,737	15,222

The cash reserve with the Central Bank of Oman cannot be withdrawn without its approval.

B 2 Due from banks and financial institutions

	2018 RO'000	2017 RO'000
Local currency (A)		
Wakalah placements with banks	**5,000**	-
Foreign currency abroad (B)		
Wakalah placements with banks	**3,884**	7,705
Demand accounts	**961**	277
Total (A+B)	**9,845**	7,982
Expected credit loss allowance	**(15)**	NA
	9,830	7,982

The analysis of changes in the gross carrying amount and corresponding ECL allowance on due from banks and financial institutions is as follows:

Gross carrying amount	**Stage 1 RO'000**	**Stage 2 RO'000**	**Stage 3 RO'000**	**Total RO'000**
As at 1 January 2018	7,982	-	-	7,982
New assets originated or purchased	9,568	-	-	9,568
Assets derecognised or repaid	(7,705)	-	-	(7,705)
Transfers to Stage 2	(5,000)	5,000	-	-
At 31 December 2018	**4,845**	**5,000**	**-**	**9,845**

ECL	**Stage 1 RO'000**	**Stage 2 RO'000**	**Stage 3 RO'000**	**Total RO'000**
As at 1 January 2018 (Note A5 i)	-	-	-	**-**
Impact of adopting IFRS 9 (Note A5 i)	5	-	-	5
Restated ECL allowance as at 1 January 2018	5	-	-	5
Net charge for the year	10	-	-	10
Transfers to Stage 2	(1)	1	-	-
At 31 December 2018	**14**	**1**	**-**	**15**

There have been no significant changes in due from banks and financial institutions gross balances, which have contributed to significant changes to the ECL over the year.

B 3 Financing advances and other receivables

	2018		
	Self-financed	**Jointly financed**	**Total**
	RO'000	**RO'000**	**RO'000**
Book value			
Murabaha receivables	**13,557**	**-**	**13,557**
Ijarah muntahia bittamleek	**19,158**	**39,125**	**58,283**
Istisna followed by Ijarah muntahia bittamleek	**61,085**	**13,041**	**74,126**
Diminishing Musharka	**34,545**	**1,957**	**36,502**
	128,345	**54,123**	**182,468**
Expected credit loss allowance	**(1,712)**	**(1,063)**	**(2,775)**
Contractual profit not recognised	**(9)**	**(60)**	**(69)**
	126,627	**53,000**	**179,624**

	2017		
	Self-financed	Jointly financed	Total
	RO'000	RO'000	RO'000
Book value			
Murabaha receivables	12,570	-	12,570
Ijarah muntahia bittamleek	22,354	32,508	54,862
Istisna followed by Ijarah muntahia bittamleek	31,057	10,366	41,423
Diminishing Musharka	35,405	2,417	37,822
	101,386	45,291	146,677
Provision for impairment – general	(1,099)	(536)	(1,635)
Provision for impairment – specific	(119)	(1)	(120)
	100,168	44,754	144,922

B 3 Financing advances and other receivables (continued)

The below table provides a comparison of provision held as per IFRS 9 and required as per CBO norms

CBO classification	IFRS 9 classification	Gross carrying amount	CBO Provision	IFRS 9 Provisions	Difference between CBO and IFRS 9	Net carrying amount	CBO Reserve interest	IFRS 9 Reserve interest
1	2	3	4	5	(6)=(4)-(5)	(7)=(3)-(5)	8	9
		RO'000	**RO'000**	**RO'000**	**RO'000**	**RO'000**	**RO'000**	**RO'000**
Standard	**Stage 1**	159,436	1,728	457	1,271	158,979	-	-
	Stage 2	21,279	216	1,231	(1,015)	20,048	-	-
	Stage 3	109	1	44	(43)	65	1	1
						-		-
Special mention	**Stage 1**	-	-	-	-	-	-	-
	Stage 2	161	2	9	(7)	152	-	-
	Stage 3	11	-	3	(3)	8	-	-
						-		-
Substandard	**Stage 1**	-	-	-	-	-	-	-
	Stage 2	-	-	-	-	-	-	-
	Stage 3	447	114	11	103	436	7	7
						-		-
Doubtful	**Stage 1**	-	-	-	-	-	-	-
	Stage 2	-	-	-	-	-	-	-
	Stage 3	987	473	975	(502)	12	61	61
						-		-
Loss	**Stage 1**	-	-	-	-	-	-	-
	Stage 2	-	-	-	-	-	-	-
	Stage 3	38	38	42	(4)	(4)	-	-
						-		
Total	**Stage 1**	159,436	1,728	457	1,271	158,979	-	-
	Stage 2	21,440	218	1,240	(1,022)	20,200	-	-
	Stage 3	1,592	626	1,075	(449)	517	69	69
	Total	**182,468**	**2,572**	**2,772**	**(200)**	**179,696**	**69**	**69**

The analysis of changes in the gross carrying amount and corresponding ECL allowance on financing advances and other receivables is as follows:

Gross carrying amount	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
	RO'000	**RO'000**	**RO'000**	**RO'000**
As at 1 January 2018	**137,355**	**7,918**	**1,424**	**146,667**
New assets originated or purchased	57,248	-	-	57,248
Assets derecognised or repaid	(19,963)	(1,662)	168	(21,457)
Transfers to Stage 1	2,698	(2,698)	-	-
Transfers to Stage 2	(17,882)	17,882	-	-
At 31 December 2018	**159,436**	**21,440**	**1,592**	**182,468**

B 3 Financing advances and other receivables (continued)

ECL	Stage 1 RO'000	Stage 2 RO'000	Stage 3 RO'000	Total RO'000
As at 1 January 2018 (Note A5 i)	-	-	-	**1,751**
Impact of adopting IFRS 9 (Note A5 i)	-	-	-	**38**
Restated ECL allowance as at 1 January 2018	**301**	**127**	**1,358**	**1,786**
Transfers to Stage 1	2	(2)	-	-
Transfers to Stage 2	(10)	10	-	-
Net charge for the year	164	1,105	(283)	**986**
At 31 December 2018	**460**	**1,240**	**1,075**	**2,775**

B 3A Murabaha receivables

	2018		
	Self-financed **RO'000**	**Jointly financed** **RO'000**	**Total** **RO'000**
Book value	**15,481**	**-**	**15,481**
Deferred profit	**(1,924)**	**-**	**(1,924)**
Net Book value	**13,557**	**-**	**13,557**
Expected credit loss allowance	**(195)**	**-**	**(195)**
Contractual profit not recognised	**(2)**	**-**	**(2)**
	13,360	**-**	**13,360**

Murabaha receivables which are Stage 3 as of 31 December 2018 amounted to RO 154 K (2017: 146 K)

	2017		
	Self-financed RO'000	Jointly financed RO'000	Total RO'000
Book value	14,275	-	14,275
Deferred profit	(1,705)	-	(1,705)
Net Book value	12,570	-	12,570
Provision for impairment - general	(221)	-	(221)
Provision for impairment - specific	(99)	-	(99)
	12,250	-	12,250

B 3B Ijarah muntahia bittamleek

	2018		
	Self-financed **RO'000**	**Jointly financed** **RO'000**	**Total** **RO'000**
Cost	**26,075**	**50,434**	**76,509**
Accumulated Depreciation	**6,917**	**11,309**	**18,226**
Net Book value	**19,158**	**39,125**	**58,283**
Expected credit loss allowance	**(152)**	**(1,021)**	**(1,173)**
Contractual profit not recognised	**(1)**	**(60)**	**(61)**
	19,005	**38,044**	**57,049**

Ijarah muntahia bittamleek which are Stage 3 as of 31 December 2018 amounted to RO 999 K (2017: RO 9K).

B 3 Financing advances and other receivables (continued)

B 3B Ijarah muntahia bittamleek (continued)

	2017		
	Self-financed	Jointly financed	Total
	RO'000	RO'000	RO'000
Cost	26,913	41,477	68,390
Accumulated Depreciation	(4,559)	(8,969)	(13,528)
Net Book value	22,354	32,508	54,862
Provision for impairment - general	(216)	(409)	(625)
Provision for impairment - specific	(9)	-	(9)
	22,129	32,099	54,228

B 3C Istisna followed by Ijarah muntahia bittamleek

	2018		
	Self-financed	**Jointly financed**	**Total**
	RO'000	**RO'000**	**RO'000**
Book value	**61,085**	**13,041**	**74,126**
Expected credit loss allowance	**(197)**	**(25)**	**(222)**
Contractual profit not recognised	**-**	**-**	**-**
	60,888	**13,016**	**73,904**

Istisna followed by Ijarah muntahia bittamleek which are Stage 3 as of 31 December 2018 amounted to RO 43 K (2017: RO 11 K)

	2017		
	Self-financed	Jointly financed	Total
	RO'000	RO'000	RO'000
Book value	31,057	10,366	41,423
Provision for impairment – general	(308)	(103)	(411)
Provision for impairment – specific	(11)	(1)	(12)
	30,738	10,262	41,000

B 3D Diminishing Musharka

	2018		
	Self-financed	**Jointly financed**	**Total**
	RO'000	**RO'000**	**RO'000**
Book value	**34,545**	**1,957**	**36,502**
Expected credit loss allowance	**(1,168)**	**(17)**	**(1,185)**
Contractual profit not recognised	**(6)**	**-**	**(6)**
	33,371	**1,940**	**35,311**

B 3 Financing advances and other receivables (continued)

B 3D Diminishing Musharka (continued)

	2017		
	Self-financed	Jointly financed	Total
	RO'000	RO'000	RO'000
Book value	35,405	2,417	37,822
Provision for impairment - general	(354)	(24)	(378)
	35,051	2,393	37,444

B 4 Investment securities

	2018	2017
	RO'000	RO'000
Held at FVTPL	**8,099**	-
Held at amortised cost	**12,890**	-
Debt securities – Sukuk		
Unquoted fixed rate debt-type investments classified at amortised cost (secured)	**-**	3,032
Quoted fixed rate debt-type investments classified at amortised cost (secured)	**-**	7,444
Unquoted fixed rate debt-type investments classified at fair value (secured)	**-**	5,328
	20,989	15,804
Expected credit loss allowance	**(45)**	-
	20,944	15,804

The Sukuk certificates are for a period of 5 years and carry profit rate of 3.5% - 8.5% per annum.

All investment securities are classified under stage 1 as of 1 January 2018 and 31 December 2018.

Movement in expected credit loss allowance is as given below:

	Stage 1	**Stage 2**	**Stage 3**	**Total**
	RO'000	**RO'000**	**RO'000**	**RO'000**
Balance at beginning of the period	**-**	**-**	**-**	**-**
Impact of adopting IFRS 9	**24**	**-**	**-**	**24**
Restated ECL allowance as at 1 January 2018	**24**	**-**	**-**	**24**
Net charge for the period	**21**	**-**	**-**	**21**
At 31 December 2018	**45**	**-**	**-**	**45**

B 5 Property, plant and equipment

	Computer software RO'000	Furniture and fixtures RO'000	Office equipment RO'000	Motor vehicle RO'000	Capital work in-progress RO'000	Total RO'000
Cost:						
At 1 January 2018	**1,100**	**600**	**454**	**99**	**62**	**2,315**
Additions	**17**	**158**	**92**	**12**	**101**	**380**
Disposals / transfers	**-**	**(72)**	**(10)**	**13**	**(62)**	**(131)**
As at 31 December 2018	**1,117**	**686**	**536**	**124**	**101**	**2,564**
Accumulated depreciation:						
At 1 January 2018	**(468)**	**(371)**	**(297)**	**(82)**	**-**	**(1,218)**
Charge for the year	**(115)**	**(91)**	**(74)**	**(13)**	**-**	**(293)**
Disposals / transfers	**-**	**66**	**10**	**(3)**	**-**	**73**
As at 31 December 2018	**(583)**	**(396)**	**(361)**	**(98)**	**-**	**(1,438)**
Net book value at 31 December 2018	**534**	**290**	**175**	**26**	**101**	**1,126**

	Computer software RO'000	Furniture and fixtures RO'000	Office equipment RO'000	Motor vehicle RO'000	Capital work in-progress RO'000	Total RO'000
Cost:						
At 1 January 2017	1,100	585	446	99	-	2,230
Additions	-	15	8	-	62	85
As at 31 December 2017	1,100	600	454	99	62	2,315
Accumulated depreciation:						
At 1 January 2017	(353)	(287)	(229)	(67)	-	(936)
Charge for the year	(115)	(84)	(68)	(15)	-	(282)
As at 31 December 2017	(468)	(371)	(297)	(82)	-	(1,218)
Net book value at 31 December 2017	632	229	157	17	62	1,097

B 6 Other assets

	2018 RO'000	2017 RO'000
Profit / rental receivable	**739**	589
Recoverable from head office	**371**	282
Advance against financing	**187**	28
Others	**1,107**	814
	2,404	1,713

B 7 Wakala deposits

	2018 RO'000	2017 RO'000
Local currency:		
-banks	**5,000**	-
-corporates & retail	**96,525**	84,944
Foreign Currency:		
-banks	**7,703**	-
-corporates & retail	**24,148**	23,517
	133,376	108,461

Wakalah deposits includes various facilities with a fixed profit rate ranging from 1.2% – 4.75 %. The maturity of the Wakalah payables ranges from 1 week to 85 months.

B 8 Customer accounts and other accounts

	2018 RO'000	2017 RO'000
Accounts by nature:		
- current	**11,257**	10,060
- margin	**7,911**	9,776
	19,168	19,836

B 9 Other liabilities

	2018 RO'000	2017 RO'000
Profit/fee payable	**82**	41
Staff entitlements	**257**	163
Payable to takaful company	**106**	184
Expected credit loss allowance on financing advance commitments and financial guarantees	**13**	-
Other accruals and provisions & payable	**1,197**	569
	1,655	957

The analysis of changes in the gross carrying amount and corresponding ECL allowance on financing advance commitments and financial guarantees is as follows:

Gross carrying amount	**Stage 1** **RO'000**	**Stage 2** **RO'000**	**Stage 3** **RO'000**	**Total** **RO'000**
Balance as at 1 January 2018	**32,570**	**-**	**-**	**32,570**
New assets originated or purchased	2,131	-	-	2,131
Assets derecognised or repaid Bal	(1,355)	-	-	(1,355)
Transfers to Stage 1	-	-	-	-
Transfers to Stage 2	-	-	-	-
Transfers to Stage 3	-	-	-	-
Amounts written off	-	-	-	-
At 31 December 2018	**33,346**	**-**	**-**	**33,346**

B 9 Other liabilities (continued)

	Stage 1 RO'000	Stage 2 RO'000	Stage 3 RO'000	Total RO'000
Balance as at the beginning of the year (A5 i)	**-**	**-**	**-**	**-**
Impact of adopting IFRS 9 (A5 i)	**7**	**-**	**-**	**7**
Restated ECL allowance as at 1 January 2018	**7**	**-**	**-**	**7**
Net charge for the period	**6**	**-**	**-**	**6**
At 31 December 2018	**13**	**-**	**-**	**13**

B 10 Equity of investment account holders

	2018 RO'000	2017 RO'000
Saving accounts	**40,736**	34,166
Term accounts	**248**	301
	40,984	34,467

B 10 Equity of investment account holders (continued)

Unrestricted investment account holder accounts are monies invested by customers under Mudaraba to form a pool of funds. Investment accountholder's funds are commingled with the Banks's funds for investment, no priority is granted to any party for the purpose of investments and distribution of profits.

Term deposits are deposits which can be withdrawn with no loss of capital subject to certain conditions.

The share, as Mudarib, in the profits of equity of investment accountholders is up to a maximum of 70% (2017: 70%) as per the terms of investment account holder agreements.

During the year, the Window has not charged any administrative expense to the pool.

Product	Participation factor	Average rate earned
Saving-OMR	17	1.75%
Saving-AED	7	0.60%
Saving-USD	7	0.57%
Term 6 Month	10	0.73%
Term 12 Months	18	1.39%

B 11 Owners' equity

(a) Assigned Capital

As required under clauses 3.5.1.2 and 3.5.1.3 of Title 1,'*Licensing Requirements*' of IBRF, the head office assigned capital of RO 10 million to the Window at inception. The head office raised this through a rights issue of shares. The head office has progressively assigned further capital into the Window and during 2018, assigned capital of RO 4 million (2017: RO 4 million) to the Window. As a result, the assigned capital of the Window as of 31 December 2018 amounted to RO 25 million (2017: RO 21 million).

(b) Legal reserve

As per Article 78 of Commercial Companies Law of Oman of 1974 'an additional amount within 2% of the nominal value of share may be collected for each share as issue fees. If the shares are issued at a value higher than the nominal value, the excess amount, after deducting issue expenses, shall be added either to the legal reserve or a special reserve to be established as provided under Article 106 of the Law'. Accordingly, the Window has transferred the net excess amount of the issue proceeds collected by the Bank during Window's inception to the legal reserve.

B 11 Owners' equity (continued)

(c) General reserve

This represents retained earnings allocated by head office.

(d) Impairment reserve

CBO circular BM 1149 requires the Window to create a reserve for the difference between provisions under CBO norms and IFRS 9 provisions, if CBO provisions are higher than IFRS 9 provisions. The provisions required under IFRS 9 are higher than the provisions computed under CBO norms as of 1 January 2018 and 31 December 2018, accordingly, no impairment reserve has been created.

B12 Contingent liabilities and commitments

B12.1 Contingent liabilities

Standby letters of credit and guarantees commit the Bank to make payments on behalf of customers' contingent upon the failure of the customer to perform under the terms of the contract.

	2018	2017
	RO'000	RO'000
Guarantees	**29,073**	24,713
Letter of credit	**3,228**	1,516
	32,301	26,229

B12.2 Commitments

Credit related commitments include commitments to extend credit, standby letters of credit and guarantees, which are designed to meet the requirements of the Bank's customers. Commitments to extend credit represent contractual commitments to make financing and advances. Commitments generally have fixed expiry dates or other termination clauses and require the payment of a fee. Since commitments may expire without being drawn upon, the total contract amounts do not necessarily represent future cash obligations.

	2018	2017
	RO'000	RO'000
Credit related commitments	**1,045**	6,341

B13 Related parties

In the ordinary course of business, the Window conducts transactions with certain of its Directors, shareholders, senior management, head office, Sharia Supervisory Board (SSB), Sharia reviewer and companies in which they have a significant interest. These transactions are conducted on an arm's length basis and are approved by the Window's management and Board of Directors.

The aggregate amount of balances and the income and expenses generated with such related parties are as follows:

	2018 RO'000	2017 RO'000
Financing and advances (balance at end of year)	**-**	32
Financing and advances disbursed during the year	**-**	115
Financing and advances repaid during the year	**(32)**	(75)
Deposits (balance at end of year)	**-**	-
Deposits received during the year	**-**	1,044
Deposits paid during the year	**-**	(1,044)
Profit on financing and advances (during the year)	**-**	28
Profit expense (during the year)	**-**	1
Senior management compensation		
Salaries and other short term benefits	**210**	222
Directors' sitting fees and remuneration		
Sharia Supervisory Board's sitting fees and remuneration	**50**	44
Transaction with head office		
Profit paid on wakala borrowings	**5**	-
Fee on committed line	**162**	147
Income on forex contracts	**-**	270

B14 Derivatives

In the ordinary course of business the Window enters into various types of transactions that involve derivative financial instruments. A derivative financial instrument is a financial contract between two parties where payments are dependent upon movements in price in one or more underlying financial instrument, reference rate or index. These derivatives are stated at fair value. The fair value of a derivative is the equivalent of the unrealised gain or loss from marking to market the derivative using prevailing market rates or internal pricing models. Unrealised gains or losses are included in the statement of comprehensive income. The derivative financial instruments used by the Window are described below:

B14.1 Derivative product types

Currency forward (Wa'ad), is a unilateral agreement between parties to buy one currency against selling another currency at an agreed price for settlement at forward/future value date. The exchange rate used for the transaction is called the forward exchange rate.

It is done to hedge from exchange rate volatility risk and to manage liquidity efficiently by allowing window to place/invest excess liquidity with offshore banks or to take funds from offshore banks in case of liquidity shortage.

As part of its asset and liability management the Window uses derivatives for hedging purposes in order to reduce its exposure to currency and profit rate risks. This is achieved by hedging specific financial instruments and forecasted transactions as well as strategic hedging against overall statement of financial position exposures.

As at 31 December 2018	**Notional**	***Notional amounts by term to maturity***		
	amount	***Within 3 months***	***3 - 12 months***	***1 - 5 years***
	RO'000	***RO'000***	***RO'000***	***RO'000***
Forward foreign exchange purchase contracts	**142,863**	**90,528**	**52,335**	**-**
Forward foreign exchange sales contracts	**142,863**	**90,528**	**52,335**	**-**

As at 31 December 2017	Notional	*Notional amounts by term to maturity*		
	amount	*Within 3 months*	*3 - 12 months*	*1 - 5 years*
	RO'000	*RO'000*	*RO'000*	*RO'000*
Forward foreign exchange purchase contracts	79,063	47,041	32,022	-
Forward foreign exchange sales contracts	79,063	47,041	32,022	-

Main counter party to forward contracts is the head office.

C 1 Income from financing activities

	31 December 2018 RO'000	31 December 2017 RO'000
Murabaha	**851**	679
Ijarah muntahia bittamleek	**3,433**	3,251
Istisna followed by Ijarah muntahia bittamleek	**3,146**	1,666
Diminishing Musharaka	**1,006**	945
	8,436	6,541
Income from jointly financed assets	**2,252**	1,992
Income from self-financed assets	**6,184**	4,549
	8,436	6,541

C 2 Income from investing activities

	31 December 2018 RO'000	31 December 2017 RO'000
Income from inter-bank placements with Islamic banks	**205**	69
Income from investment in debt-type instruments	**930**	614
	1,135	683

C 3 Profit paid

	31 December 2018 RO'000	31 December 2017 RO'000
On Mudaraba deposit	**744**	392
On Wakala deposit-		
-Customers	**3,868**	2,869
-Banks	**302**	190
	4,170	3,059
	4,914	3,451

C 4 Other income (net)

	31 December 2018 RO'000	31 December 2017 RO'000
Fee and commission – net	**555**	476
Loss on held for trading investment securities - realised	**(285)**	-
Others	**(7)**	-
	263	476

C 5 Other operating expenses

	31 December 2018 RO'000	31 December 2017 RO'000
Operating and administration costs	**1,114**	724
Establishment costs	**277**	217
SSB remuneration and sitting fees	**50**	44
	1,441	985

D Financial risk management

D1 Credit risk

D1.1 Credit risk in financing products

Credit risk originates from the financing of receivables and leases (including but not limited to, Murabaha, Diminishing Musharaka, Istisna and Ijarah) and financing of working capital (including but not limited to Salam). Windows acts as financier, supplier, Rabb-ul-Mal and contributor of capital in Musharaka agreement. Window exposes itself with the risk of counterparty's failure to meet their obligations in terms of receiving deferred payment and making or taking delivery of an asset.

The Window manages and controls credit risk by setting limits on the extent of risk it is willing to accept in terms of amounts, counterparties, product types, geographical area and industry sector. It has established a credit quality review process to provide early identification of possible changes in the creditworthiness of counterparties, including regular collateral revisions. Counterparty limits are established by the use of a credit risk classification system, which assigns each counterparty a risk rating. Risk ratings are subject to regular revision by the Credit Review and Analysis Department ("CR&AD"). Any changes to the Credit Risk Policy will be approved by the Board.

Exposure limits are based on the aggregate exposure to counterparty and any connected entities. Corporate contracts/facilities are reviewed on an annual basis by CR&AD.

To cover unforeseen risk, which dries up the cash flows, additional tangible investments are taken as collateral such as real estate or equity shares. The Window implements guidelines on the acceptability of specific classes of collateral credit risk mitigation. The principal types of collaterals for financings and advances are:

- charges of assets under murabaha agreements
- ownership/title of assets under Ijarah & Istisna financing
- ownership/title under Istisna arrangement

D1.2 Management of credit risk

All financings and advances of the Window are regularly monitored to ensure compliance with the stipulated repayment terms. Those financings and advances are classified into one of the 5 risk classification categories: Standard, Special Mention, Substandard, Doubtful and Loss – as stipulated by Central Bank of Oman regulations and guidelines. The responsibility for identifying problem accounts and classifying them rests with the business line functions.

D Financial risk management (continued)

D1 Credit risk (continued)

D1.2 Management of credit risk (continued)

The credit exposure of the Window as on the reporting date is as follows:

31 December 2018	**Murabaha receivables**	**Ijarah muntahia bittamleek**	**Istisna followed by Ijarah muntahia bittamleek**	**Diminishing Musharka**	**Wakala placements & balance with banks**	**Debt type securities**	**Total**
In (RO'000)							
Stage 1	**12,966**	**54,328**	**73,285**	**18,858**	**9,845**	**20,989**	**190,271**
Stage 2	**437**	**2,956**	**798**	**17,249**	**-**	**-**	**21,440**
Stage 3	**154**	**999**	**43**	**396**	**-**	**-**	**1,592**
Total	**13,557**	**58,283**	**74,126**	**36,503**	**9,845**	**20,989**	**213,303**

31 December 2017	Murabaha receivables	Ijarah muntahia bittamleek	Istisna followed by Ijarah muntahia bittamleek	Diminishing Musharka	Wakala placements & balance with banks	Debt type securities	Total
In (RO'000)							
Stage 1	11,887	48,384	39,718	37,347	7,982	15,804	161,122
Stage 2	401	5,380	1,661	475	-	-	7,917
Stage 3	282	1,098	44	-	-	-	1,424
Total	12,570	54,862	41,423	37,822	7,982	15,804	170,463

D1.2 Management of credit risk

Maximum exposure to credit risk before collateral held or other credit enhancements for all on-balance sheet assets are based on net carrying amounts as reported in the statement of financial position.

The maximum credit risk exposures relating to off-balance sheet items calculated as per Basel II guidelines are provided in note D6. The amounts represented in the note D6 represent a worst case scenario of credit risk exposure as of 31 December 2018, without taking into account any collateral held or other credit enhancements attached.

D Financial risk management (continued)

D1 Credit risk (continued)

D1.3 Credit rating analysis

The table below presents an analysis of debt securities, treasury bills, gross placements and other eligible bills by rating agency designation at 31 December 2018, based on Moody's ratings or equivalent.

	2018 RO'000	2017 RO'000
A1 to A3	**4,845**	5,779
Baa1 to Baa3	**5,000**	10,286
Ba+ to B-	**8,099**	-
Sovereign	**12,845**	7,444
	30,789	23,509

The Window performs an independent assessment based on quantitative and qualitative factors in cases where a counter party is unrated.

The Bank's internal credit rating grades along with the respective PDs are as below:

Internal rating grades	Internal rating grade description	PD range (%)
1 – 6	Investment grade	0.10% to 2.00%
7	Sub-investment grade	3.70%
8 - 10	Non-performing	6.60% to 20.00%

The table below shows the credit quality by class of financial asset, based on internal credit ratings:

31 December 2018	**Murabaha receivables**	**Ijarah muntahia bittamleek**	**Istisna followed by Ijarah muntahia bittamleek**	**Diminishing Musharka**	**Wakala placements & balance with banks**	**Debt type securities**	**Total**
In (RO'000)							
Stage 1 (12 month ECL)							
Investment grade	**12,966**	**54,328**	**73,285**	**18,858**	**9,845**	**20,989**	**190,271**
Sub-investment grade	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Carrying amount	**12,966**	**54,328**	**73,285**	**18,858**	**9,845**	**20,989**	**190,271**
Stage 2 (Lifetime ECL but not credit-impaired)							
Investment grade	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Sub-investment grade	**437**	**2,956**	**798**	**17,249**	**-**	**-**	**21,440**
Carrying amount	**437**	**2,956**	**798**	**17,249**	**-**	**-**	**21,440**
Stage 3 (Lifetime ECL and credit-impaired)							
Impaired	**154**	**999**	**43**	**396**	**-**	**-**	**1,592**
	13,557	**58,283**	**74,126**	**36,503**	**9,845**	**20,989**	**213,303**

D Financial risk management (continued)

D1 Credit risk (continued)

D1.3 Credit rating analysis (continued)

1 January 2018 In (RO'000)	Murabaha receivables	Ijarah muntahia bittamleek	Istisna followed by Ijarah muntahia bittamleek	Diminishing Musharka	Wakala placements & balance with banks	Debt type securities	Total
Stage 1 (12 month ECL)							
Investment grade	11,887	48,384	39,718	37,347	7,892	15,804	161,122
Sub-investment grade	-	-	-	-	-	-	-
Carrying amount	11,887	48,384	39,718	37,347	7,892	15,804	161,122
Stage 2 (Lifetime ECL but not credit-impaired)							
Investment grade	-	-	-	-	-	-	-
Sub-investment grade	401	5,380	1,661	475	-	-	7,917
Carrying amount	401	5,380	1,661	475	-	-	7,917
Stage 3 (Lifetime ECL and credit-impaired)							
Impaired	282	1,098	44	-	-	-	1,424
Carrying amount	12,570	54,862	41,423	37,822	7,892	15,804	170,463

D1.4 Allowances for impairment

The Window establishes an allowance for impairment losses account that represents its estimate of incurred losses in its financing and advances portfolio. The components of this allowance are specific loss components that relate to individually significant exposures and a collective financing and advances loss allowance established for group of homogenous assets in respect of losses that have been incurred but have not been identified on financings subject to individual assessment for impairment

D1.5 Write-off policy

The Window writes off a financing and advances/security balance (and any related allowances for impairment losses) when the Window determines that the financing and advances/security is uncollectible. This determination is reached after considering information such as the occurrence of significant changes in the borrower/issuer's financial position such that the borrower/issuer can no longer repay the obligation, or that proceeds from the collateral will not be sufficient to pay back the entire exposure. For smaller balance standardized financings, charge off decisions generally are based on a product specific past due status.

The assets, or title to the asset, will be maintained in the Window's custody or with a custodian approved by the Window. Necessary measures are taken to ensure that the assets are maintained in useable condition.

The release of collateral without full repayment of all related financial obligations requires authorization of the same level that originally approved and sanctioned the facility. Substitution of collateral is permitted if the new collateral would further minimize the Window's risk exposure keeping in mind the regulatory requirements.

When collateral is released to the customer, the Credit Administration Department obtains and maintains in its records acknowledgement of receipt from the customer or its authorized representative.

An estimate of the fair value of collateral and other security enhancements held against financings and advances is shown below:

	2018	2017
	RO'000	RO'000
Property	**355,505**	131,796
Equity	**-**	12,425
	355,505	144,221

Settlement risk is the risk of loss due to the failure of a party to honor its obligations to deliver cash, investments or other assets as contractually agreed on the day of settlement.

In foreign exchange trades, though there is fulfilment of both the legs of the transaction on the settlement date as is common practice between trading partners (free settlement), there will be risk on account of different time zones. In these cases, the settlement risk is mitigated through the execution of bilateral payment netting agreements.

D1.6 Concentrations

Concentrations of credit risk arise when a number of counter parties are engaged in similar business activities or activities in the same geographic region or have similar economic features that would cause their ability to meet contractual obligations to be affected similarly by changes in economic, political or other conditions. Concentrations of credit risk indicate the relative sensitivity of the Window's performance to developments affecting a particular industry or geographic location.

In order to avoid excessive concentrations of risk, the Window's policies and procedures include specific guidelines to focus on maintaining a diversified portfolio. Identified concentrations of credit risks are controlled and managed accordingly.

D Financial risk management (continued)

D1 Credit risk (continued)

D1.6 Concentrations (continued)

- Regulatory Caps – exposure limits to a person (including juristic person) and his connected parties has been set at 15% of the Bank's Net worth.
- Net worth is the aggregate amount of assets less liabilities, which shall include assets and liabilities both within and outside the Sultanate.
- Exposure to senior member in the management of the Window and any related parties shall not exceed 10% of the amount of the net worth of the Bank and aggregate of all such exposures shall not exceed 35% of the amount of the net worth.

Limits are not applicable to exposures fully secured by cash or cash equivalent (not subject to withdrawal from the Window) or are secured by guarantee of the financial institutions within or outside Sultanate of Oman or the Government of the Sultanate of Oman.

	2018					
	Murabaha	**Ijara**	**Istisna followed by Ijarah muntahia bittamleek**	**Diminishing Musharka**	**Due from banks**	**Investment securities**
	RO'000	**RO'000**	**RO'000**	**RO'000**	**RO'000**	**RO'000**
Concentration by sector						
Corporate	**1,460**	**18,818**	**60,630**	**32,323**	**-**	**8,099**
Personal	**11,900**	**38,231**	**13,274**	**2,988**	**-**	**-**
Sovereign	**-**	**-**	**-**	**-**	**-**	**12,845**
Banks	**-**	**-**	**-**	**-**	**9,830**	**-**
	13,360	**57,049**	**73,904**	**35,311**	**9,830**	**20,944**
Concentration by location						
Middle east	**13,360**	**57,049**	**73,904**	**35,311**	**5,140**	**20,944**
Europe	**-**	**-**	**-**	**-**	**4,690**	**-**
North America	**-**	**-**	**-**	**-**	**-**	**-**
Asia	**-**	**-**	**-**	**-**	**-**	**-**
Total	**13,360**	**57,049**	**73,904**	**35,311**	**9,830**	**20,944**

D Financial risk management (continued)

D1 Credit risk (continued)

D1.6 Concentrations (continued)

	2017					
	Murabaha	Ijara	Istisna followed by Ijarah muntahia bittamleek	Diminishing Musharka	Due from banks	Investment securities
	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
Concentration by sector						
Corporate	2,508	23,808	30,735	36,940	-	8,360
Personal	9,742	30,420	10,265	504	-	-
Sovereign	-	-	-	-	-	7,444
Banks	-	-	-	-	7,982	
	12,250	54,228	41,000	37,444	7,982	15,804
Concentration by location						
Middle east	12,250	54,228	41,000	37,444	4,004	15,804
Europe	-	-	-	-	82	-
North America	-	-	-	-	42	-
Asia	-	-	-	-	3,854	-
Total	12,250	54,228	41,000	37,444	7,982	15,804

D2 Liquidity risk

Liquidity risk is the risk that the Window will encounter difficulty in meeting its obligations associated with its financial liabilities that are settled by delivering cash or another financial asset.

D2.1 Management of liquidity risk

The Window's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions without incurring unacceptable losses or risking damage to the Bank's reputation.

Window's central treasury receives information from other business units regarding the liquidity profile of their financial assets and liabilities and details of other projected cash flows arising from projected future business. Central treasury then maintains a portfolio of short-term liquid assets, largely made up of short-term liquid investment securities, financing and advances and advances to banks and other inter-bank facilities, to ensure that sufficient liquidity is maintained within the Bank as a whole. The liquidity requirements of business units are met through short-term financing and advances from central treasury to cover any short-term fluctuations and longer term funding to address any structural liquidity requirements. The Bank has also laid down a comprehensive liquidity contingency plan for effective management of liquidity. In this process due care is taken to ensure that the Window complies with all the CBO regulations.

All liquidity policies and procedures are subject to review and approved by Asset Liabilities Committee (ALCO). Computation of liquidity gap on maturity of assets and liabilities is provided. The computation has been prepared in accordance with guidelines provided by the regulator.

The lending ratio, which is the ratio of the total financings and advances to customer deposits and capital, is monitored on a daily basis in line with the regulatory guidelines. Internally the lending ratio is set at a more conservative basis than required by regulation. The Window also manages its liquidity risk on regular basis and by monitoring the liquid ratio which is a ratio of net liquid assets to total assets on a monthly basis. For this purpose net liquid assets are considered as including cash and cash equivalents and investment grade debt investments for which there is an active and liquid market.

D Financial risk management (continued)

D2 Liquidity risk (continued)

D2.1 Management of liquidity risk (continued)

Details of the reported lending and liquid ratio as at 31 December 2018 were as follows:

	2018	
	Lending ratio	**Liquid ratio**
Average for the year	**84.27%**	**8.32%**
Maximum for the year	**85.84%**	**11.14%**
Minimum for the year	**78.31%**	**3.30%**

	2017	
	Lending ratio	Liquid ratio
Average for the year	84.87%	9.46%
Maximum for the year	85.44%	21.02%
Minimum for the year	84.11%	2.37%

The table below summarizes the maturity profile of the Window's liabilities as on the reporting date based on contractual repayment arrangements. The contractual maturities of assets and liabilities have been determined on the basis of the remaining period at the statement of financial position date to the contractual maturity date and do not take account of the effective maturities as indicated by the Window's deposit retention history and the availability of liquid funds.

D2.2 Exposure to liquidity risk

2018	**Carrying amount RO'000**	**Within three months RO'000**	**Four months to 12 months RO'000**	**One to three years RO'000**	**More than three years RO'000**	**Total RO'000**
Wakala deposits	**133,376**	**31,263**	**74,564**	**27,613**	**4,207**	**137,647**
Customer deposit and other accounts	**19,168**	**-**	**-**	**-**	**19,168**	**19,168**
Other liabilities	**1,655**	**-**	**-**	**-**	**1,655**	**1,655**
	154,199	**31,263**	**74,564**	**27,613**	**25,030**	**158,470**
Equity of Investment account holders	**40,984**	**213**	**36**	**-**	**40,736**	**40,985**
	195,183	**31,476**	**74,600**	**27,613**	**65,766**	**199,455**

D Financial risk management (continued)

D2 Liquidity risk (continued)

D2.2 Exposure to liquidity risk (continued)

2017	Carrying amount RO'000	Within three months RO'000	Four months to 12 months RO'000	One to three years RO'000	More than three years RO'000	Total RO'000
Wakala deposits	108,461	47,758	23,189	41,091	98	112,136
Customer deposit and other accounts	19,836	19,836	-	-	-	19,836
Other liabilities	957	957	-	-	-	957
	129,254	68,551	23,189	41,091	98	132,929
Equity of Investment account holders	34,467	34,467	-	-	-	34,467
	163,721	103,018	23,189	41,091	98	167,396

The Window prepares a liquidity gap report to monitor the Window's short term liquidity position on the Rial denominated assets and liabilities in a time horizon spanning one month. The gap is adjusted for availability of instruments for repo or refinance and also for unavailed committed lines of credit, if any. This statement of short term liquidity is to be reported to the ALCO every month.

In addition to the above measures of liquidity, the window also monitors the Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio as per the regulator in line with Basel-III standards.

D3 Market risk

Market risk is the exposure to loss resulting from the changes in the profit rates, foreign currency exchange rates, equity prices and commodity prices. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return to risk.

D3.1 Market risk in financing products

Financing contracts mainly comprise 'Murabaha receivables' and 'Ijara Muntahia Bittamleek'. Following are the financing related market risk:

Murabaha receivables

In the case of an asset in possession for a Murabaha transaction and an asset acquired specifically for resale to a customer in a non-binding Murabaha to the purchase ordered (MPO) transaction, the asset would be treated as inventory of the Window and is subject to price risk.

Ijara Muntahia Bittamleek (IMB)

In the case of Non-binding Promise to lease an asset acquired and held for the purpose of either operating Ijarah or IMB. The asset would be treated as asset owned by the Window and is subject to price risk from its acquisition date until its disposal.

D Financial risk management (continued)

D3 Market risk (continued)

D3.2 Measurement of market risk

The Window is mainly engaged in Spots and Currency swaps. Since the positions are taken mainly for customer transactions, the complexity is further reduced. In view of above, the Window measures and controls the risk by using a limit framework. As and when the Window enters into more complex derivatives, it will have more sophisticated models and techniques to measure market risk, supported by a suitable mechanism.

D3.3 Management of market risks

The Window separates its exposure to market risk between trading and non -trading portfolios. Trading portfolios include all positions arising from market making and proprietary position taking, together with financial assets and liabilities that are managed on a fair value basis.

All foreign exchange risk within the Window is transferred by Central Treasury to the trading book. Accordingly, the foreign exchange position is treated as a part of the Window's trading portfolio for risk management purposes. Foreign currency risk is monitored and managed by the Window by establishment of Middle Office to monitor the market risk, and the risk is managed by putting in place Policy, and implementing limit framework, reporting tools like Currency Position Report, Risk Analysis of Currency Position, Breach Analysis Report, and Dealer Limit Breach report.

Overall authority for market risk is vested in ALCO. The risk management function is responsible for development of detailed risk management policies (subject to approval by ALCO and Risk Management Committee of the Board). The Policy is periodically reviewed to keep it up to date with the market developments.

D3.4 Exposure to profit rate risk

Profit rate risk is the potential impact of the mismatch between the rate of return on assets and the expected rate of funding due to the sources of finance. Senior management identifies the sources of profit rate risk exposures based upon the current as well as forecasted balance sheet structure of Window. The profit rate risk in the Window may arise due to the following transactions:

- Murabaha transactions;
- Wakala transactions;
- Isitisna followed by Ijara Muntahia Bittamleek
- Ijara Muntahia Bittamleek;
- Istisna;
- Sukuk; and
- Musharaka investments.

Window's management believes that the Window is not exposed to material profit rate risk as the re-pricing of assets, liabilities and equity of investment accountholders occur at similar intervals. The profit distribution to equity of investment accountholders is based on profit sharing agreements. Therefore, Window is not subject to any significant profit rate risk.

Sources of Profit Rate Risk
The different profit rate risks faced by the Window can be classified broadly into the following categories.

- Re-pricing risk which arises from timing differences in the maturity (for fixed rate) and re-pricing (for floating rate) of assets, liabilities and off balance sheet positions. As profit rates vary, these re-pricing mismatches expose Window's income and underlying economic value to unanticipated fluctuations;
- Yield curve risk which arises when unanticipated shifts of the yield curve have adverse effects on Window's income and/or underlying economic value;
- Basis risk which arises from imperfect correlation in the adjustment in the rate earned on products priced and the rate paid on different instruments with otherwise similar re-pricing characteristics. When profit rates change, these differences can give rise to unexpected changes in the cash flows and earnings spread

between assets, liabilities, and off balance sheet instruments of similar maturities or re-pricing frequencies; and

D Financial risk management (continued)

D3 Market risk (continued)

D3.4 Exposure to profit rate risk (continued)

Sources of Profit Rate Risk (continued)

- Displaced Commercial Risk refers to the market pressure to pay returns that exceeds the rate that has been earned on the assets financed by the liabilities, when the return on assets is under performing as compared to competitor's rates.

Profit rate risk strategy
Profit rate risk arises from the possibility that changes in profit rates will affect future profitability or the fair values of financial instruments. The window is exposed to profit rate risk as a result of mismatches or gaps in the amounts of assets and liabilities and off-balance sheet instruments that mature or re-price in a given period. The window manages this risk through risk management strategies.

The effective profit rate (effective yield) of a monetary financial instrument is the rate that, when used in a present value calculation, results in the carrying amount of the instrument. The rate is a historical rate for a fixed rate instrument carried at amortized cost and a current rate for a floating rate instrument or an instrument carried at fair value.

Profit rate risk measurement tools
Window monitors Re-pricing gap analysis which measures the arithmetic difference between the profit-sensitive assets and liabilities of book in absolute terms.

Profit rate risk monitoring and reporting
Window has implemented information systems for monitoring, controlling and reporting profit rate risk. Reports are provided on a timely basis to Executive Committee and the Board of Directors of the head office.

The Risk and Compliance Unit monitors these limits regularly. They reviews the results of gap limits and exceptions, if any, and recommends corrective action to be taken which is approved by ALCO or Executive Committee, according to authority parameters approved by the Board.

D Financial risk management (continued)

D3 Market risk (continued)

D3.5 Exposure to profit rate risk – non trading portfolios

The Window's profit sensitivity position based on contractual re-pricing arrangements at 31 December 2018 was as follows:

	Effective annual Profit Rate %	Within three months RO'000	Four months to 12 months RO'000	Over one year RO'000	Non sensitive to profit rate RO'000	Total RO'000
At 31 December 2018						
Assets						
Cash and balances with central bank		-	-	-	8,737	8,737
Due from banks and financial institutions	2.53	8,871	-	-	959	9,830
Murabaha receivables	5.77	-	-	-	13,363	13,363
Ijarah muntahia bittamleek	5.20	22,443	-	34,606	-	57,049
Istisna followed by Ijarah muntahia bittamleek	5.41	13,985	-	59,919	-	73,904
Diminishing Musharka	4.94	4,515	-	30,796	-	35,311
Investment securities	4.78	-	-	20,944	-	20,944
Fixed assets		-	-	-	1,126	1,126
Other assets		-	-	-	2,401	2,401
Total assets		49,814	-	146,265	26,586	222,665
Liabilities and equity						
Wakala deposits	3.67	33,719	96,197	3,460	-	133,376
Customer current accounts		-	-	-	19,168	19,168
Other liabilities		-	-	-	1,655	1,655
Total liabilities		33,719	96,197	3,460	20,823	154,199
Equity of Investment account holders	1.75	40,984	-	-	-	40,984
Total liabilities and equity of Unrestricted Investment Account (URIA)		74,703	96,197	3,460	20,823	195,183
Total profit rate sensitivity gap		(24,889)	(96,197)	142,805	5,763	
Cumulative profit rate sensitivity gap		(24,889)	(121,086)	21,719	27,482	

D Financial risk management (continued)

D3 Market risk (continued)

D3.5 Exposure to profit rate risk – non trading portfolios (continued)

	Effective annual Profit Rate %	Within three months RO'000	Four months to 12 months RO'000	Over one year RO'000	Non sensitive to profit rate RO'000	Total RO'000
At 31 December 2017						
Assets						
Cash and balances with central bank		-	-	-	15,222	15,222
Due from banks and financial institutions	1.51	7,700	-	-	282	7,982
Murabaha receivables	6.23	-	-	-	12,250	12,250
Ijarah muntahia bittamleek	4.95	9,846	25,957	18,425	-	54,228
Istisna followed by Ijarah muntahia bittamleek	5.34	7,658	26,350	6,992	-	41,000
Diminishing Musharka	4.93	20,354	17,090	-	-	37,444
Investment securities	4.60		15,804	-	-	15,804
Fixed assets		-	-	-	1,097	1,097
Other assets		-	-	-	1,173	1,173
Total assets		45,558	85,201	25,417	30,024	186,200
Liabilities and equity						
Wakala deposits	3.14	47,561	22,659	38,241	-	108,461
Customer current accounts		-	-	-	19,836	19,836
Other liabilities		-	-	-	957	957
Total liabilities		47,561	22,659	38,241	20,793	129,254
Equity of Investment Account Holders	2.08	34,467	-	-	-	34,467
Total liabilities and equity of Unrestricted Investment Account (URIA)		82,028	22,659	38,241	20,793	163,721
Total profit rate sensitivity gap		(36,470)	62,542	(12,824)	9,771	23,019
Cumulative profit rate sensitivity gap		(36,470)	26,072	13,248	23,019	25,869

D Financial risk management (continued)

D3 Market risk (continued)

D 3.6 Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Board has set limits on the overall open position and for open position for each currency. The open position limits include overnight open position and intraday open position. Open positions are monitored on a daily basis and hedging strategies used to ensure positions are maintained within established limits. The Window had the following net exposures denominated in foreign currencies:

	2018		
	Assets	**Liabilities & URIA**	**Net assets**
Riyal Omani	**148,579**	**68,724**	**79,855**
United States Dollar	**72,991**	**83,757**	**(10,766)**
Euro	**1,720**	**1,716**	**4**
UAE Dirhams	**714**	**1**	**713**
Pound Sterling	**14**	**-**	**14**

	2017		
	Assets	Liabilities & URIA	Net assets
Riyal Omani	144,263	68,066	46,197
United States Dollar	41,357	61,184	-19,827
Euro	76	1	75
UAE Dirhams	954	1	953
Pound Sterling	89	2	87

The Window takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Board sets limits on the level of exposure by currency and in aggregate for both overnight and intra-day positions, which are monitored daily.

Changes in the non-parity foreign currency prices as at 31 December 2018 and 2017 on net assets is considered negligible.

D4 Operational risk

Operational risk is defined as the risk of direct or indirect loss resulting from inadequate or failed internal processes, people and systems or from external events. Operational risk arises due to variety of causes associated with the Window's processes, personnel, technology and infrastructure and from external events and to include risks other than credit, market and liquidity risks.

Window has adopted same policies and procedures to mitigate operational risk as those of the head office. Advantages of head office processes and infrastructure are obtained in compliance with IBRF. Policies on following processes are also similar to that of the head office:

- Track loss events and potential exposures;
- Reporting of losses, indicators and scenarios on a regular basis; and
- Review the reports jointly by risk and line managers;

In addition to the above, Window has a dedicated Sharia' compliance officer responsible to ensure compliance with IBRF, Sharia' guidelines and other applicable laws and regulations.

D Financial risk management (continued)

D5 Displaced commercial risk

Displaced commercial risk ("DCR") refers to the magnitude of risks that are transferred to shareholders in order to cushion the Investment Account Holder ("IAH") from bearing some or all of the risks to which they are contractually exposed in Mudaraba contracts.

Under a Mudaraba (profit sharing and loss-bearing) contract, unrestricted IAH are exposed to aggregate impact of risks arising from the assets in which their funds are invested, but this is managed by Sohar Islamic Window through DCR.

This risk-sharing is achieved by constituting and using various reserves such as PER, and by adjusting the Sohar Islamic Window's profit share in order to smooth the returns payable to the IAH from exposure to the volatility of aggregate returns arising from banking risks, and thereby to enable payment of returns that are competitive in the marketplace.

Sohar Islamic Window manages its displaced commercial risk as outlined in its Profit Distribution Policy. The Window foregoes its fee in case displaced commercial risk arises. The Window manages profit rates with other Islamic Windows and full-fledged Islamic/ Conventional Banks operating in Oman.

D6 Capital management

D6.1 Regulatory capital

The Window's lead regulator, Central Bank of Oman, sets and monitors capital requirements for the Window as a whole. In implementing current capital requirements Central Bank of Oman requires the Window to maintain a prescribed ratio of total capital to total risk-weighted assets. The Window calculates capital requirements for market risk and operational risk based upon the model prescribed by Central Bank of Oman as follows:

- Sovereign entities – Nil for Oman
  Window's – Risk weighting based upon ratings by external credit assessment institutions as approved by CBO
- Retail and Corporate financings - As per credit conversion factors and risk weightage prescribed by Central Bank of Oman.
- Off balance sheet items – As per credit conversion factors and risk weightage prescribed by Central Bank of Oman.

The Window's regulatory capital is analysed into three tiers:

- Tier 1 capital, which includes allocated capital and reserves, retained earnings and intangible assets, and other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes.

- Tier 2 capital, which includes qualifying collective impairment allowances

Various limits are applied to elements of the capital base. The amount of innovative tier 1 investments cannot exceed 15 percent of total tier 1 capital; qualifying tier 2 capital cannot exceed tier 1 capital; and qualifying term subordinated financing and advances capital may not exceed 50 percent of tier 1 capital. There are also restrictions on the amount of collective impairment allowances, PER and IRR that may be included as part of tier 2 capital. Other deductions from capital include the carrying amounts of investments in subsidiaries that are not included in the regulatory consolidation, investments in the capital of Windows and certain other regulatory items.

Window's operations are categorized as either trading book or banking book, and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and off-balance sheet exposures. There is no availability of data for previous three years as required under basic indicator approach for computation of capital charge for operational risk. The Window's policy is to maintain a strong capital base.

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

D Financial risk management (continued)

D6 Capital management (continued)

D6.1 Regulatory capital (continued)

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

	2018 RO'000	2017 RO'000
Tier 1 capital		
Assigned capital	**25,000**	21,000
Legal reserve	**134**	134
General reserve	**988**	988
Retained earnings	**1,360**	897
Total	**27,482**	23,019
Tier 2 capital		
Impairment allowance on portfolio basis	**1,510**	1,635
Total	**1,510**	1,635
Total regulatory capital	**28,992**	24,654
Risk-weighted assets		
Window credit and market risk	**197,310**	154,344
Operational risk	**7,779**	5,413
Total risk-weighted assets	**205,090**	159,751
Capital adequacy ratio		
Total regulatory capital expressed as a percentage of total risk-weighted assets	**14.14%**	15.43%
Total tier 1 capital expressed as a percentage of total risk-weighted assets	**13.40%**	14.41%

The capital adequacy ratio given above is calculated in accordance with the Basel II norms as adopted by Central Bank of Oman and IBRF.

D7 Segmental information

The activities of the Window are performed as one unit. Reporting to management is made by business unit. The Window operates solely in the Sultanate of Oman and as such no geographical segment information is presented.

D8 Other disclosures

Following are the disclosures required under Islamic Banking Regulatory Framework:

- There has been no comingling of the funds.
- As of 31 December 2018, and amount of RO 382 thousands is payable to head office.
- During the year head office has allocated RO 641 thousands (2017: RO 258 thousands) cost for shared services.
- There has been no amount transferred to Charity fund during the year.
- Proposed remuneration and sitting fee of SSB board is as follows:

			RO
Name	**Remuneration**	**Sitting Fee**	**Total**
Dr. Hussain Hamed Hassan	15,400	6,160	21,560
Dr. Mudassir Siddiqui	11,550	6,160	17,710
Sheikh Azzan bin Nasir Farfoor Al Amri	7,700	6,160	13,860
Sheikh Fahad Mohamed Hilal Al Khalili	7,700	6,160	13,860
	42,350	24,640	66,990