NATIONAL BANK OF OMAN (SAOG)-
UAE BRANCHES

Financial statements

31 December 2013

National Bank of Oman (SAOG), UAE Branches

Financial statements
31 December 2013

Contents

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Independent auditors' report

The Country Manager
National Bank of Oman (SAOG), UAE Branches

Report on the financial statements

We have audited the accompanying financial statements of National Bank of Oman (SAOG), UAE Branches ("the Branches") which comprise the statement of financial position as at 31 December 2013, statement of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, and for such internal controls as management determines is necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error.

Auditors' responsibility

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

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

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

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Branches as at 31 December 2013, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Report on other legal and regulatory requirements

We further confirm that we have obtained all information and explanations necessary for our audit and that the financial statements comply, in all material respects, with the applicable requirements of Union Law No. 10 of 1980.

KPMG

29 APR 2014

KPMG Lower Gulf limited
Munther Dajani
Registration No. 268

National Bank of Oman (SAOG), UAE Branches

Statement of financial position

As at 31 December

	Note	2013 AED'000	2012 AED'000
Assets			
Cash and balances with the UAE Central Bank	8	**103,753**	73,807
Due from banks	9	**121,638**	135,577
Due from Head Office and overseas branches	25	**19,839**	24,282
Customers' indebtedness for acceptances	27	**16,404**	10,530
Loans and advances to customers	5(b)	**295,773**	283,194
Investment securities	10	**25,757**	-
Property and equipment	11	**2,924**	2,731
Other assets	12	**4,210**	2,270
Total assets		**590,298**	532,391
Liabilities			
Due to Head Office and overseas branches	25	**73,274**	89,599
Deposits from customers	13	**366,095**	298,951
Liabilities under acceptances	27	**16,404**	10,530
Other liabilities	14	**8,734**	7,544
Total liabilities		**464,507**	406,624
Equity			
Branch capital	15	**52,500**	52,500
Legal reserve	16	**25,295**	25,293
Retained earnings		**20,696**	20,674
Total equity		**98,491**	98,467
Funding from Head Office			
Placement from Head Office	17 & 25	**27,300**	27,300
Total equity and funding from Head Office		**125,791**	125,767
Total Liabilities, Equity and Funding from Head Office		**590,298**	532,391
Commitments and contingent liabilities	26	**468,922**	294,255

Salaam ~~Said~~ Al Shaksy
Chief Executive Officer

Manoj S Nair
Country Manager-UAE

The attached notes 1 to 28 form part of these financial statements.

The independent auditors' report is set out on page 1.

National Bank of Oman (SAOG), UAE Branches

Statement of profit or loss and other comprehensive income ('OCI')

for the year ended 31 December

	Note	2013 AED'000	2012 AED'000
Operating income			
Interest income	*18*	**17,430**	18,101
Interest expense	*18*	**(5,066)**	(6,048)
Net interest income	*18*	**12,364**	12,053
Net fees and commission income	*19*	**5,594**	3,676
		17,958	15,729
Net foreign exchange gain		**1,316**	958
Other operating income	*20*	**1,393**	1,375
Total operating income		**20,667**	18,062
Operating expenses			
Staff costs		**(10,360)**	(8,188)
Depreciation	*11*	**(1,190)**	(1,209)
Other operating expenses	*21*	**(6,447)**	(5,566)
Total operating expenses		**(17,997)**	(14,963)
Profit from operations before impairment losses		**2,670**	3,099
Provision for credit losses, net	*5(b)*	**(2,640)**	1,575
Profit before income tax		**30**	4,674
Income tax expense, net	*22*	**(6)**	(519)
Profit		**24**	4,155
Other comprehensive income		**-**	-
Total comprehensive income		**24**	4,155

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National Bank of Oman (SAOG), UAE Branches

Statement of changes in equity

for the year ended 31 December

	Share capital AED'000	Legal reserve AED'000	Retained earnings AED'000	Total AED'000
At 1 January 2012	52,500	24,877	16,935	94,312
Total comprehensive income for the year	-	-	4,155	4,155
Transfer to legal reserve	-	416	(416)	-
At 31 December 2012	52,500	25,293	20,674	98,467
At 1 January 2013	52,500	25,293	20,674	98,467
Total comprehensive income for the year	-	-	24	24
Transfer to legal reserve	-	2	(2)	-
At 31 December 2013	**52,500**	**25,295**	**20,696**	**98,491**

The attached notes 1 to 28 form part of these financial statements.
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National Bank of Oman (SAOG), UAE Branches

Statement of cash flows

for the year ended 31 December

	Note	2013 AED'000	2012 AED'000
Cash flows from operating activities			
Profit before income tax		**30**	4,674
Adjustments for:			
Depreciation	*11*	**1,190**	1,209
Provision for credit losses	*5(b)*	**12,450**	10,296
Provision for employees' end-of-service benefits	*23*	**161**	307
Loss on disposal of property and equipment		**-**	12
		13,831	16,498
Changes in:			
Due from Head Office and overseas branches		**20,971**	(23,875)
Loans and advances to customers		**(129)**	66,926
Customers' indebtedness for acceptances		**(5,874)**	(5,824)
Other assets		**(1,940)**	(5,689)
Due to Head Office and overseas branches		**(32,853)**	(49,586)
Deposits from customers		**67,144**	684
Liabilities under acceptances		**5,874**	5,824
Other liabilities		**1,190**	6,170
Net cash generated from operating activities		**68,214**	11,128
Income tax paid		**(935)**	(1,895)
End-of-service benefits paid	*23*	**(482)**	(119)
Net cash from operating activities		**66,797**	9,114
Cash flows from Investing activities			
Purchase of property and equipment	*11*	**(1,382)**	(2,754)
Purchase of investment securities		**(25,757)**	-
Net cash used in investing activities		**(27,139)**	(2,754)
Net increase in cash and cash equivalents		**39,658**	6,360
Cash and cash equivalents at 1 January		**144,066**	137,706
Cash and cash equivalents at 31 December	*24*	**183,724**	144,066

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1 Legal status and activities

National Bank of Oman SAOG (the "Bank" or the "Head Office") was established in the Sultanate of Oman in 1973 as a joint stock company and is engaged in retail banking, wholesale banking and investment banking services. The UAE Branches (the "Branches") operate in the United Arab Emirates ("UAE") under a commercial bank license granted by the UAE Central Bank. The registered office of the Branch is P O Box 3822, Abu Dhabi, UAE.

The principal activities of the Branches are the granting of loans, advances and the provision of other commercial banking services.

The financial statements were authorised for issue by the Branches' management on 29 APR 2014.

2 Basis of preparation

2.1 *Statement of compliance*

These financial statements have been prepared in accordance with guidelines of the UAE Central Bank and the International Financial Reporting Standards (IFRSs), as issued by the International Accounting Standards Board (IASB).

2.2 *Basis of measurement*

The financial statements have been prepared on a historical cost basis except for derivative financial instruments and investment securities, which are stated at fair value.

2.3 *Functional and presentation currency*

These financial statements have been presented using UAE Dirham ("AED"), which is the functional currency of the Branches. Except as otherwise indicated, financial information presented in AED has been rounded to the nearest thousand.

2.4 *Significant accounting judgments and estimates*

In preparing these financial statements, management has made judgments, estimates and assumptions that affect the application of the accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised prospectively.

Going concern

The Branches management has made an assessment of the Branches ability to continue as a going concern and is satisfied that the Branches have the resources to continue in business for the foreseeable future. Furthermore, the management is not aware of any material uncertainties that may cast significant doubt upon the Branches ability to continue as a going concern. Therefore, the financial statements continue to be prepared on the going concern basis.

2.4 *Significant accounting judgments and estimates (continued)*

Impairment losses on loans and advances and investment securities

Assets accounted for at amortised cost are evaluated for impairment on the basis described in Note 4.

The Branches reviews its individually significant loans and advances at each reporting date to assess whether an impairment loss should be recorded in the statement of comprehensive income. In particular, judgment by management is required in the estimation of the amount and timing of future cash flows when determining the impairment loss. In estimating these cash flows, the Branch makes judgments about the borrower's financial situation and the net realisable value of collateral. These estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the allowance.

Loans and advances that have been assessed individually and found not to be impaired and all individually insignificant loans and advances are then assessed collectively, in groups of assets with similar risk characteristics, to determine whether provision should be made due to incurred loss events for which there is objective evidence but whose effects are not yet evident. The collective assessment takes account of data from the loan portfolio (such as credit quality, levels of arrears, credit utilisation, loan to collateral ratios etc.) and concentrations of risks.

In making an assessment of whether an investment in sovereign debt is impaired, the Branches consider 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, about governments' and agencies' willingness 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 fulfill the required criteria.

Fair value measurement principles

The 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. Consequently, differences can arise between carrying values and the fair value estimates.

While these financial statements are prepared under the historical cost convention modified for measurement at fair value of derivatives and available-for-sale investments, in the opinion of management, the carrying values and fair values of those financial assets and liabilities that are not carried at fair value in the financial statements are not materially different, since assets and liabilities are either short term in nature or frequently repriced.

The Branches use the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;
Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and
Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

At 31 December 2013 and 2012, the Branches used level 1 valuation hierarchy for its available-for-sale investments and level 2 for its derivative financial instruments.

3 Changes in accounting policies

Except for the changes below, the Branches have consistently applied the accounting policies set out in note 4 to all periods presented in these financial statements.

The Branches have adopted the following new relevant standards and amendments to standards, including any consequential amendments to other standards, with a date of initial application of 1 January 2013.

(a) *IFRS 13 - Fair value measurement*

IFRS 13 establishes a single framework for measuring fair value and making disclosures about fair value measurements when such measurements are required or permitted by other IFRSs. It unifies the definition of fair value as 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. It replaces and expands the disclosure requirements about fair value measurements in other IFRSs, including IFRS 7. The change had no significant impact on the measurement of the Branches' assets and liabilities.

(b) *Presentation of items of Other Comprehensive Income (Amendments to IAS 1)*

The amendments to IAS 1 introduce a grouping of items presented in other comprehensive income (OCI). Items that could be reclassified (or recycled) to profit or loss at a future point in time now have to be presented separately from items that will never be reclassified. The change had no significant impact on the presentation of the Branches' OCI for the current or comparative period.

4 Significant accounting policies

a) Foreign currency

Transactions in foreign currencies are translated into the functional currency of the Branches at the spot exchange rates at the date of the transactions.

Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated 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 the amortised cost in the functional currency at the beginning of the year, adjusted for effective interest and payments during the year, and the amortised cost in the foreign currency translated at the spot exchange rate at the end of the year.

Non-monetary assets and liabilities that are measured at fair value in a foreign currency are translated into the functional currency at the spot exchange rate at the date on which the fair value is determined. Non-monetary items that are measured based on historical cost in a foreign currency are translated using the spot exchange rate at the date of the transaction.
Foreign currency differences arising on translation are generally recognised in profit and loss.

b) Interest

Interest income and expense are recognised in profit or loss using the effective interest method. The 'effective interest rate' is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or financial liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Branches estimate future cash flows considering all contractual terms of the financial instrument, but not future credit losses.

The calculation of the effective interest rate includes all transaction costs, fees and points paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or liability.

4 Significant accounting policies *(continued)*

c) Fees and commission income

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

Other fees and commission income – including account servicing fees, investment management fees, sales commission, placement fees and syndication fees – are recognised as the related services are performed. If a loan commitment is not expected to result in the draw-down of a loan, then the related loan commitment fees are recognised on a straight-line basis over the commitment period.

Other fees and commission expense relate mainly to transaction and service fees, which are expensed as the services are received.

d) Leases

Lease payments – lessee

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

e) Taxation

Taxation is provided for in accordance with the instructions of the Department of Private Affairs of His Highness Shaikh Zayed Bin Sultan Al Nahyan, dated 11 September 2003.

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

f) Financial assets and financial liabilities

(i) Recognition

The Branches initially recognise loans and advances and deposits on the date on which they are 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 Branches becomes a party to the contractual provisions of the instrument.

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

(ii) Classification

Financial assets

The Branches classifies its financial assets into one of the following categories:
- held for trading;
- loans and receivables; and
- available-for-sale

Financial liabilities

The Branches classify their financial liabilities, other than financial guarantees and loan commitments, as measured at amortised cost.

(iii) Derecognition

Financial assets

The Branches derecognise a financial asset when the contractual rights to the cash flows from the financial asset expire, or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership of the financial asset are transferred or in which the Branches neither transfer nor retain substantially all of the risks and rewards of ownership and do not retain control of the financial asset.

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognised) and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in OCI is recognised in profit or loss. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Branches is recognised as a separate asset or liability.

4 Significant accounting policies *(continued)*

f) Financial assets and liabilities (continued)

Derecognition (*continued*)

When the Branches have transferred their rights to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Branches continuing involvement in the asset. In that case, the Branches 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 Branch 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 Branches could be required to repay.

Financial liabilities

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

The Branches derocognise a financial liability when its contractual obligation are discharged or cancelled, or expires.

(iv) Offsetting

Financial assets and financial liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Branches have a legal right to set off the amounts and intend either to settle them 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 under IFRS, or for gains and losses arising from a group of similar transactions.

(v) Amortised cost measurement

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

(vi) Fair value measurement

Policy applicable from 1 January 2013

When available, the Branches measure the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

If there is no quoted price in an active market, then the Branches use valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The chosen valuation technique incorporates all of the factors that market participants would take into account in pricing a transaction.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price – i.e. the fair value of the consideration given or received. If the Branches determine that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique that uses only data from observable markets, then the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price. Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is wholly supported by observable market data or the transaction is closed out.

4 Significant accounting policies *(continued)*

(vi) Fair value measurement ***(continued)***

If an asset or a liability measured at fair value has a bid price and an ask price, then the Branches measure assets and long positions at a bid price and liabilities and short positions at an ask price.

Portfolios of financial assets and financial liabilities that are exposed to market risk and credit risk that are managed by the Branches on the basis of the net exposure to either market or credit risk are measured on the basis of a price that would be received to sell a net long position (or paid to transfer a net short position) for a particular risk exposure. Those portfolio-level adjustments are allocated to the individual assets and liabilities on the basis of the relative risk adjustment of each of the individual instruments in the portfolio.

The fair value of a demand deposit is not less than the amount payable on demand, discounted from the first date on which the amount could be required to be paid.

The Branches recognise transfers between levels of the fair value hierarchy as of the end of the reporting period during which the change has occurred.

Policy applicable before 1 January 2013

'Fair value' is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction on the measurement date.

When available, the Branches measure the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If a market for a financial instrument is not active, then the Branches establish fair value using a valuation technique. The chosen valuation technique makes maximum use of market inputs, relies as little as possible on estimates specific to the Branches, incorporates all factors that market participants would consider in setting a price and is consistent with accepted economic methodologies for pricing financial instruments.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price – i.e. the fair value of the consideration given or received. However, in some cases the initial estimate of fair value of a financial instrument on initial recognition may be different from its transaction price. If this estimated fair value is evidenced by comparison with other observable current market transactions in the same instrument (without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets, then the difference is recognised in profit or loss on initial recognition of the instrument. In other cases, the fair value at initial recognition is considered to be the transaction price and the difference is not recognised in profit or loss immediately but is recognised over the life of the instrument on an appropriate basis or when the instrument is redeemed, transferred or sold, or the fair value becomes observable.

If an asset or a liability measured at fair value has a bid price and an ask price, then the Branches measure assets and long positions at a bid price and liabilities and short positions at an ask price. Where the Branches have positions with offsetting risks, mid-market prices are used to measure the offsetting risk positions and a bid or ask price adjustment is applied only to the net open position as appropriate.

The fair value of a demand deposit is not less than the amount payable on demand, discounted from the first date on which the amount could be required to be paid.

4 Significant accounting policies (*continued*)

(vii) Identification and measurement of impairment

At each reporting date, the Branches assess whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. A financial asset or a group of financial assets is impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset(s) and that the loss event has an impact on the future cash flows of the asset(s) that can be estimated reliably.

Objective evidence that financial assets are impaired includes:

- significant financial difficulty of the borrower or issuer;
- default or delinquency by a borrower;
- the restructuring of a loan or advance by the Branches on terms that the Branches would not consider otherwise;
- indications that a borrower or issuer will enter bankruptcy;
- observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group.

The Branches consider evidence of impairment for loans and advances and held-to-maturity investment securities at both a specific asset and a collective level. All individually significant loans and advances and held-to-maturity investment securities are assessed for specific impairment. Those found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Loans and advances and held-to-maturity investment securities that are not individually significant are collectively assessed for impairment by grouping together loans and advances and held-to-maturity investment securities with similar risk characteristics.

In assessing collective impairment the Branches use the higher of 1.5% of risk weighted asset computed as per Central Bank of UAE guidelines and a statistical modelling which incorporates historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical modelling. Default rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

Impairment losses on assets measured at amortised cost are calculated as the difference between the carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate.

Impairment losses are recognised in profit or loss and reflected in an allowance account against loans and receivables or held-to-maturity investment securities. Interest on the impaired assets continues to be recognised through the unwinding of the discount. If an event occurring after the impairment was recognised causes the amount of impairment loss to decrease, then the decrease in impairment loss is reversed through profit or loss.

Impairment losses on available-for-sale investment securities are recognised by reclassifying the losses accumulated in the fair value reserve in equity to profit or loss. The cumulative loss that is reclassified from equity to profit or loss is the difference between the acquisition cost, net of any principal repayment and amortisation, and the current fair value, less any impairment loss recognised previously in profit or loss. Changes in impairment attributable to application of the effective interest method are reflected as a component of interest income.

If, in a subsequent period, the fair value of an impaired available-for-sale debt security increases and the increase can be related objectively to an event occurring after the impairment loss was recognised, then the impairment loss is reversed through profit or loss; otherwise, any increase in fair value is recognised through OCI. Any subsequent recovery in the fair value of an impaired available-for-sale equity security is always recognised in OCI.

The Branches writes off a loan or an investment debt security, either partially or in full, and any related allowance for impairment losses, when management determines that there is no realistic prospect of recovery.

4 Significant accounting policies *(continued)*

g) Cash and cash equivalents

'Cash and cash equivalents' include notes and coins on hand, unrestricted balances held with central banks and highly liquid financial assets with original maturities of three months or less from the acquisition date that are subject to an insignificant risk of changes in their fair value, and are used by the Branches in the management of their short-term commitments.

h) Loans and advances

'Loans and advances' are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Branches does not intend to sell immediately or in the near term.

Loans and advances to banks and loans and advances to customers are classified as loans and receivables.

Loans and advances are initially measured at fair value plus incremental direct transaction costs, and subsequently measured at their amortised cost using the effective interest method. When the Branches chooses to designate the loans and advances as measured at fair value through profit or loss they are measured at fair value with face value changes recognised immediately in profit or loss.

i) Investment securities

Investment securities are initially measured at fair value plus, in the case of investment securities not at fair value through profit or loss, incremental direct transaction costs, and subsequently accounted for depending on their classification as either held to maturity, fair value through profit or loss, or available-for-sale.

Available-for-sale

Available-for-sale investments' are non-derivative investments that are designated as available-for-sale or are not classified as another category of financial assets. Available-for-sale investments comprise equity securities and debt securities. Unquoted equity securities whose fair value cannot be measured reliably are carried at cost. All other available-for-sale investments are measured at fair value after initial recognition.

Interest income is recognised in profit or loss using the effective interest method. Dividend income is recognised in profit or loss when the Branches becomes entitled to the dividend. Foreign exchange gains or losses on available-for-sale debt security investments are recognised in profit or loss. Impairment losses are recognised in profit or loss.

4 Significant accounting policies *(continued)*

i) Investment securities *(continued)*

Available-for-sale (continued)

Other fair value changes, other than impairment losses, are recognised in OCI and presented in the fair value reserve within equity. When the investment is sold, the gain or loss accumulated in equity is reclassified to profit or loss.

A non-derivative financial asset may be reclassified from the available-for-sale category to the loans and receivables category if it would otherwise have met the definition of loans and receivables and if the Branches has the intention and ability to hold that financial asset for the foreseeable future or until maturity.

j) Property and equipment

(i) Recognition and measurement

Items of property and equipment are measured at cost less accumulated depreciation and any accumulated impairment losses.

If significant parts of an item of property or equipment have different useful lives, then they are accounted for as separate items (major components) of property and equipment.

Any gain or loss on disposal of an item of property and equipment (calculated as the difference between the net proceeds from disposal and the carrying amount of the item) is recognised within other income in profit or loss.

(ii) Subsequent costs

Subsequent expenditure is capitalised only when it is probable that the future economic benefits of the expenditure will flow to the Branches. Ongoing repairs and maintenance are expensed as incurred.

(iii) Depreciation

Depreciation is calculated to write off the cost of items of property and equipment less their estimated residual values using the straight-line method over their estimated useful lives, and is generally recognised in profit or loss. Leased assets are depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that the Branches will obtain ownership by the end of the lease term. Land is not depreciated.

The estimated useful lives of significant items of property and equipment are as follows:

· Leasehold improvements	3 to 5 years
· Motor vehicles	4 years
· Furniture	10 years
· Equipment	5 years

Depreciation methods, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

k) Impairment of non-financial assets

The carrying amounts of the Branches' non financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash generating unit is the smallest identifiable asset category that generates cash flows that largely are independent from other assets. Impairment losses are recognised in the statement of comprehensive income.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

4 Summary of significant accounting policies *(continued)*

k) Impairment of non-financial assets *(continued)*

Impairment losses are recognised in profit or loss. They are allocated first to reduce the carrying amount of any goodwill allocated to the CGU, and then to reduce the carrying amounts of the other assets in the CGU on a pro rata basis.

l) Provisions

A provision is recognised if, as a result of a past event, the Branches 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 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 risks specific to the liability. The unwinding of the discount is recognised as finance cost.

m) Staff terminal benefits

The terminal benefits are provided for in accordance with the employees' contracts of employment and applicable requirements of the UAE and Oman labour laws. Entitlement to these benefits is usually based upon the employees' length of service and completion of minimum service period. The expected costs of these benefits are accrued over the period of employment.

n) Segment reporting

The Branches segmental reporting is based on the following operating segments: Commercial banking and treasury and investments. Segment results are reported to the Chief Executive Officer of the Bank, (being the chief operating decision maker) and include items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

o) New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning after 1 January 2013, and have not been applied in preparing these financial statements. Those that may be relevant to the Branches are set out below. The Branches does not plan to adopt these standards early.

- IFRS 9 Financial Instruments (2013) - *Effective date unannounced as yet*
- Offsetting Financial Assets and Financial Liabilities (Amendments to IAS 32) - *Effective for annual periods beginning on or after 1 January 2014*

5 Financial risk management

a) Introduction and overview

The Branches have exposure to the following risks from its use of financial instruments:

- credit risk;
- liquidity risk;
- market risks; and
- operational risks

This note presents information about the Branches exposure to each of the above risks, the Branches objectives, risk management frameworks, policies and processes for measuring and managing risk, and the Branches' management of capital.

Risk management framework

The overall responsibility for risk management in the Branches is vested with the Board of Directors of the Bank. The Board authorises appropriate credit, liquidity and market risk policies as well as suitable operational guidelines based on the recommendation of management. Approval authorities are delegated to different functionaries, including the UAE Country Manager, in the hierarchy depending on the amount, type of risk and collateral security. The Bank has established various committees that decide on all risk issues.

b) Credit risk

Credit risk is the risk of financial loss to the Branches if a customer or counterparty to a financial instrument fails to meet its contractual obligations. The Branches seek to manage its credit risk exposure through diversification of lending activities to avoid undue concentrations of risks with individuals or groups of customers in specific locations or businesses. The Branches also monitor credit exposures and continually assesses the credit worthiness of counterparties. They also obtain security when appropriate.

Management of credit risk

The Board of Directors of the Bank has delegated responsibility for the oversight of credit risk to its Credit Committee. A separate Credit Department, reporting to the Credit Committee, is responsible for managing credit risk, including the following:

- Formulating credit policies in consultation with business units, covering collateral requirements, credit assessment, risk grading and reporting, documentary and legal procedures, and compliance with regulatory and statutory requirements.

- Establishing the authorisation structure for the approval and renewal of credit facilities.

- Reviewing and assessing credit risk exposures in excess of designated limits, before facilities are committed to customers by the business unit concerned. Renewals and reviews of facilities are subject to the same review process.

- Limiting concentrations of exposure to counterparties, geographies and industries (for loans and advances, financial guarantees and similar exposures), and by issuer, credit rating band, market liquidity and country (for investment securities).

- Developing and maintaining risk grading to categorise exposures according to the degree of risk of financial loss faced and to focus management on the attendant risks. The risk grading system is used in determining where impairment provisions may be required against specific credit exposures. The current risk grading framework consists of eight grades reflecting varying degrees of risk of default and the availability of collateral or other credit risk mitigation. The responsibility for setting risk grades lies with the final approving executive or committee, as appropriate. Risk grades are subject to regular reviews by Group Risk.

5 Financial risk management *(continued)*

Management of credit risk *(continued)*

• Reviewing compliance of business units with agreed exposure limits, including those for selected industries, country risk and product types. Regular reports on the credit quality of local portfolios are provided to the Credit Committee, which may require appropriate corrective action to be taken.

• Providing advice, guidance and specialist skills to business units to promote best practice throughout the Bank in the management of credit risk.

Each business unit is required to implement the credit policies and procedures, with credit approval authorities delegated from the Credit Committee. Each business unit has a Chief Credit Risk officer who reports on all credit-related matters to local management and the Credit Committee. Each business unit is responsible for the quality and performance of its credit portfolio and for monitoring and controlling all credit risks in its portfolios, including those subject to central approval.

Regular audits of business units and credit processes are undertaken by Internal Audit.

The credit quality of financial assets is managed by the Branches using internal credit ratings. The table below shows the credit quality by class of asset, based on the Branches' credit rating system. The amounts presented are gross of impairment provisions.

5 Financial risk management *(continued)*

b) Credit risk *(continued)*

Exposure to credit risk

The Branches measure their exposure to credit risk by reference to the gross carrying amount of financial assets less amounts offset, interest suspended and impairment losses, if any.

	Loans and advances		Due from banks		Investment securities	
	2013	2012	**2013**	2012	**2013**	2012
	AED'000	AED'000	**AED'000**	AED'000	**AED'000**	AED'000
Carrying amount, net	**295,773**	283,194	**121,638**	135,577	**25,757**	-
Individually impaired						
Substandard	**1**	165	-	-	-	-
Doubtful	**224**	84,297	-	-	-	-
Loss	**72,279**	37,448	-	-	-	-
Gross amount	**72,504**	121,910	-	-	-	-
Interest suspended	**(31,700)**	(31,916)	-	-	-	-
Specific allowance for impairment	**(41,105)**	(42,975)	-	-	-	-
Carrying amount*	**(301)**	47,019	-	-	-	-
Past due but not impaired (overdue by more than 90 days)	-	-	-	-	-	-
	-	-	-	-	-	-
Neither past due nor impaired						
Standard	**296,769**	242,740	**121,638**	135,577	**25,757**	-
Accounts with renegotiated terms	**7,081**	-	-	-	-	-
	303,850	242,740	**121,638**	135,577		
Total non-impaired portfolio	**303,850**	242,740	**121,638**	135,577	**25,757**	-
Collective allowance for impairment	**(7,776)**	(6,565)	-	-	-	-
Carrying amount	**296,074**	236,175	**121,638**	135,577	**25,757**	-
Carrying amount	**295,773**	283,194	**121,638**	135,577	**25,757**	-

* The negative carrying amount represents specific provision against unfunded exposures.