BASEL II PILLAR III AND BASEL III Report

31 December 2020

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

We have performed the procedures agreed with you and as prescribed in the Central Bank of Oman (CBO) Circular No. BM 1027 dated 4 December 2007 with respect to the Basel II - Pillar III Disclosures and Basel III related Disclosures (the disclosures) of Ahli Bank SAOG (the Bank) set out on pages 1 to 38 as at and for the year ended 31 December 2020. The disclosures were prepared by the management in accordance with the CBO's Circular No. BM 1009 dated 13 September 2006, Circular No. BM 1027 dated 4 December 2007, Circular No. BM 1114 dated 17 November 2013, Circular No. BM 1149 dated 13 April 2017 amended with letter BSD/CB/FLC/2018/17 dated 26 November 2018, letter BSD/CB/2020/001 dated 18 March 2020 and letter BSD/CB/2020/005 dated 3 June 2020. Our engagement was undertaken in accordance with the International Standard on Related Services applicable to agreed-upon-procedures engagements. The procedures, as set out in Circular No. BM 1027 dated 4 December 2007, were performed solely to assist you in evaluating the Bank's compliance with the disclosure requirements set out in CBO's Circular No. BM 1009 dated 13 September 2006, BM 1114 dated 17 November 2013, Circular No. BM 1149 dated 13 April 2017 amended with letter BSD/CB/FLC/2018/17 dated 26 November 2018, letter BSD/CB/2020/001 dated 18 March 2020 and letter BSD/CB/2020/005 dated 3 June 2020.

We report our findings as follows:

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

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

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

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

Our obligations in respect of this report are entirely separate from, and our responsibility and liability is in no way changed by, any other role we may have (or may have had) as auditors of the Bank or otherwise. Nothing in this report, nor anything said or done in the course of or in connection with the services, will extend any duty of care we may have in our capacity as auditors of any financial statements of the Bank.

9 March 2021
Muscat, Sultanate of Oman

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BASEL II PILLAR III AND BASEL III Report

31 December 2020

1. INTRODUCTION

This report represents the Basel II Pillar III and Basel III qualitative and quantitative disclosures, highlighting the capital adequacy, risk profile and control process of ahlibank SAOG ("the Bank") as per the requirements of CBO. The disclosures are intended to complement the Pillar I, minimum capital requirements and Pillar II, supervisory review process of the framework. They should be read in conjunction with the financial statements as of 31st December 2020.

The Bank has a formal "Disclosure Policy" for disclosure of information that it makes available to the general public as well as to the regulatory bodies. This policy is framed to enhance transparency about its activities and promote good governance. The Bank makes information publicly available in accordance with its policy on disclosure of information and applicable regulations.

Outbreak of Coronavirus (Covid-19)

The World Health Organization officially declared Covid-19 as a global pandemic on 11 March 2020. From the latter half of Q1-2020, the economic environment and business landscape of the bank have witnessed rapid changes because of the unprecedented outbreak of Coronavirus pandemic coupled with the significant depression in the global crude oil prices. Tightening of market conditions, lockdowns, restrictions on trade and movement of people have caused significant disruptions to businesses and economic activities globally and across industries and sectors.

Governments and regulatory authorities across the globe have implemented several measures to contain the impact of the spread of the virus. In line with this, the Central Bank of Oman (CBO), also instituted a host of measures to protect the stability of country's economy. These measures include deferral of loan instalments for the affected borrowers (particularly the corporates and SMEs), deferment and waiver of interest/profit for affected Omani nationals employed in private sector, waiver of point of sale (POS) charges, lowering of regulatory capital ratios and increasing the lending ratio etc., (refer CBO circular no. BSD/CB/2020/001for details). The related further details are provided in note 37 on the financial statements with regard to impact of Covid19 and various measures taken by the Bank on it.

2. SCOPE

The Bank prepares this report in accordance with the Basel Accord in conjunction with and as per the directive of the Central Bank of Oman (CBO).

The Scope of application covers the Bank only and is not part of any group either as a member or as top corporate entity in the group.

3. CAPITAL STRUCTURE

The capital base for complying with regulatory purposes differs from accounting capital. The Bank's regulatory capital is classified into two categories- Tier I and Tier II capital.

Tier 1 capital is composed of core capital and is further classified into Common Equity Tier 1 capital ('CET1') and Additional Tier 1 capital ('AT1'). CET1 includes paid up capital, legal reserves and retained earnings reduced by cumulative unrealized losses on FVOCI investments and any other applicable deduction specified in the Basel III Capital Accord. AT1 capital consists of perpetual capital instruments.

Tier II capital consists of revaluation reserves/cumulative fair value gain or losses on fair value through other comprehensive income (FVOCI) instruments, Stage 1 and Stage 2 expected credit loss allowance as allowed by CBO and subordinated debt.

There is no innovative or complex capital instrument in the capital structure of the Bank.

BASEL II PILLAR III AND BASEL III Report *(continued)*

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3. CAPITAL STRUCTURE *(Continued)*

CAPITAL MANAGEMENT

The primary objective of the Bank's Capital management framework is to ensure stability by maintaining adequate amount of high quality capital to commensurate its risk profile. Healthy levels of capital, support the Bank in attaining strong credit rating and maximizing shareholders value. The framework ensures compliance with regulatory capital requirements set by CBO.

The Bank has following credit ratings at present:

Capital Intelligence	
Foreign currency Long Term Rating:	**BB+**
Foreign currency Short term;	**B**
Outlook:	**Negative**

Fitch	
Viability rating;	**b+**
Long term foreign currency and local currency IDRs;	**B+**
Short term foreign currency and local currency IDRs; B	**B**
Support rating; 4 Outlook;	**Negative**

The process of assessing the capital requirements of the Bank commences with the compilation of the annual business plan by individual business units, which are then consolidated into the annual budget plan of the Bank. The annual budget plan provides an estimate of the overall growth in assets, its impact on capital and targeted profitability.

Strategic business objectives and future capital needs are assessed within this framework. Normally, the Bank employs capital rationing techniques to allocate capital for each of the Bank's business risk departments in order to optimize returns.

Sources of future capital are identified and plans put in place to raise and retain capital, under the terms of the framework. The Bank also manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Bank may adjust the amount of dividend payment to shareholders or issue capital to shareholders or issue capital securities.

The Bank's Finance department monitors and reports the planned versus actual position, to ensure that the Bank is always adequately capitalized. Risk weighted assets and capital are monitored by the Risk Management department also periodically to assess the quantum of capital available to support assets growth and optimally deploy capital to achieve targeted returns.

The Bank's capital structure as at 31 December 2020, based on the CBO guidelines is as follows:

Sl.No	Elements of Capital	Amount(RO'000)
	Tier I Capital	
1	Share capital*	164,966
2	Legal reserves	34,028
3	Subordinated debt reserve	11,400
4	Retained earnings*	37,149
	Common Equity Tier I before deductions	**247,543**
	Deductions:	
5	Cumulative unrealized losses and intangibles recognized directly in equity	(8,499)
	Common Equity Tier 1	**239,044**
	Additional Tier I Capital	
	Tier 1 perpetual subordinated bonds	124,000
	Tier I capital after all deductions	**363,044**
	Tier II Capital	
7	Revaluation reserves / cumulative fair value gains on FVOCI Instruments	2,719
8	Stage 1 & Stage 2 expected credit losses	19,129
9	Subordinated debt	600
	Total Tier II Capital	**22,448**
	Total Regulatory Capital	**385,492**

* The Board of Directors has proposed a cash dividend of 5%, which has been adjusted and is subject to CBO approval and shareholder approval in the AGM.

BASEL II PILLAR III AND BASEL III Report *(continued)*

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3. CAPITAL STRUCTURE *(Continued)*

CAPITAL ADEQUACY

Qualitative disclosures

The Bank's capital management framework sets out to define, measure, raise and deploy capital in a co-ordinated and consistent manner. Its objective is to maximize its return on capital and, at the same time, provide an adequate cushion to cover any unexpected losses. The Bank manages its capital in an integrated manner with the aim of maintaining strong capital ratios and high ratings. This calls for a balanced approach: maintaining capital levels that are sufficient to provide a high return to shareholders; meeting the requirements of regulators, rating agencies and other stakeholders (including deposit holders and senior creditors), and supporting future business growth. The cost of capital and its composition in terms of its quality and stability is also considered.

The capital management process of Islamic window is aligned with the strategic planning process of the Bank. Capital planning is carried out in conjunction with the strategic business and financial planning exercise. Bank maintains a five year rolling strategic plan which is updated and reviewed by the Board of Directors on an annual basis. Capital requirements are assessed based on projected business plans and budget. The Bank uses a prudential building-block approach as the measurement technique to assess capital adequacy for current and future activities, which is compared with the consolidated eligible capital.

The Bank's total capital adequacy ratio is 15.67% as against the CBO's prescribed minimum requirement of 12.25% (Including capital conversion buffer of 1.25%) as at 31 December 2020. The Bank follows a capital adequacy framework to link the Bank's annual budget projections and the capital required to achieve business objectives. It is determined by the Bank's strategic planning objectives and capital planning framework. Capital requirements are assessed for credit, operational and market risks. In order to calculate the capital adequacy ratio, the Bank follows the standardized approach forming part of the Pillar 1 requirements of Basel II Norms and adopts rating from CBO's recognized four External Credit Assessment Institutions (ECAI), namely Moody's, Standard & Poors, Fitch and Capital Intelligence, for calculating the risk on its sovereign and bank exposures. In order to equip the requirements of the advanced approaches, the Bank has already implemented obligor rating models and the ratings are being tracked regularly.

In order to meet with Pillar 2 requirements of Basel II Norms, the Bank has in place Internal Capital Adequacy Assessment Process (ICAAP) for assessing the Bank's capital adequacy in relation to various risks such as interest rate risk, liquidity risk, concentration risk etc., as well as a strategy for maintaining the capital adequacy level. Based on the guidelines issued by Central Bank of Oman, assessment under ICAAP has been completed for the years from 2020-2023 and it has been determined that the Bank is adequately capitalized to undertake its planned business activities.

ICAAP process is divided into a base case and stressed scenarios. The Bank has assumed three different kinds of stress scenarios, namely Mild, Medium and Severe. These stress scenarios differ in terms of stress event impact level (Mild being the lowest and Severe being the highest).

The following stress scenarios are applied:

- Rise in NPL by % of direct credit facilities
- Portion of SME sector performing loans become NPLs
- Decline in prices of the Bank's portfolio of investments
- Appreciation / depreciation of local currency against all other currencies
- Withdrawal of customer deposits
- Decline in liquid assets
- Shift in LIBOR yield curve
- Increase in cost of funding due to reputational risk
- Branch generated less than expected profitability
- Consolidated impact of different scenarios

In addition to the above, the Bank has also identified additional stress scenarios to include testing of expected credit losses under IFRS 9.

BASEL II PILLAR III AND BASEL III Report *(continued)*

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3. CAPITAL STRUCTURE *(Continued)*

Quantitative disclosures

i) Position of various risk weighted assets is presented as under (RO '000):

As on 31 December 2020

Sl. No	Details	Gross balances (book value)	Net balances (book value)	Risk weighted assets
1	On-balances sheet items	2,754,589	2,636,434	2,183,071
2	Off-balance sheet items	88,432	88,432	84,293
3	Derivatives	5,696	5,696	2,950
4	Market risk	-	-	72,689
5	Operational Risk	-	-	117,449
	Total			**2,460,452**
6	Tier 1 capital			363,044
7	Tier 2 capital			22,448
8	**Total Regulatory Capital**			**385,492**
8.1	Capital requirement for credit risk			278,114
8.2	Capital requirement for market risk			8,904
8.3	Capital requirement for operational risk			14,387
	Total required capital			**301,405**
9	**CET 1 ratio**			**9.72%**
10	Tier 1 ratio			**14.76%**
11	Total capital ratio			**15.67%**

ii) Capital adequacy

As on 31 December 2020

Sl. No	Details	Simple Approach
1	Tier I capital (after supervisory deductions)	364,544
2	Tier II capital (after supervisory deductions and up to eligible limits)	22,448
3	Risk weighted assets – banking book	2,270,314
4	Risk weighted assets – operational risk	117,449
5	**Total Risk Weighted Assets – Banking Book + Operational Risk**	**2,387,763**
6	**Minimum required capital to support RWAs of banking book and operational risk**	**292,501**
	i) Minimum required Tier I capital for banking book and operational risk	244,746
	ii) Tier II capital required for banking book and operational risk	47,755
7	Tier I capital available for supporting trading book	92,991
8	Tier II capital available for supporting trading book	-
9	**Risk Weighted Assets – trading book**	**72,689**
10	Total capital required to support trading book	8,904
11	Minimum Tier I capital required for supporting trading book	**2,538**
12	**Total Regulatory Capital**	**385,492**
13	**Total Risk Weighted Assets – Whole bank**	**2,460,452**
14	**BIS Capital Adequacy Ratio**	**15.67%**

BASEL II PILLAR III AND BASEL III Report *(continued)*

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3. CAPITAL STRUCTURE *(Continued)*

In order to smoothen the higher volatility in ECL computation and its impact on regulatory capital of the banks amid covid-19 outbreak, CBO has issued a new requirement to apply a "prudential filter" approach on IFRS 9 expected credit loss (ECL) provisions on calculating the regulatory capital. Any increase in the Stage 2 provisioning compared to December 31, 2019 will be added back to regulatory capital while these provisions will be gradually phased-in during a five-year period ending 31 December 2024.

Besides, the bank has also applied in its capital adequacy calculations the "Prudential filter" under interim adjustment arrangement for Stage-1 and Stage-2 ECL, as mentioned above. The impact of above filter on the bank's regulatory capital is 10 bps. Although above measures are not exhaustive and may not fully counteract the impact of COVID-19 in the short run, they will mitigate the long-term negative impact of the pandemic. In response to this crisis, the Bank continues to monitor and respond to all liquidity and funding requirements. As at the reporting date the capital position of the Bank remains strong and is well placed to absorb the impact of the current disruption.

4. RISK EXPOSURE AND ASSESSMENT

Risk Management Principles

Risk is an inherent part of the Bank's business activities. The primary goal of risk management is to ensure that the Bank's asset and liability profile, its trading positions and its credit and operational activities do not expose it to losses that could threaten its survival. Risk Management assists in ensuring that risk exposures do not become excessive, relative to the Bank's capital and financial positions. The Bank has already in place a risk appetite statement set by the Board.

The Bank manages the risks effectively and efficiently by making risk management an integral part of commercial banking business. This emphasizes a clear understanding of business requirements in terms of products, clients, delivery capabilities, competition, regulatory environment, shareholder values and the global economic environment leading the Bank to identifying the various associated risks.

Having identified the risks, the Risk Management Department formulate policies and procedures taking into account regulatory requirements and best international practices, so as to monitor and control the risks within pre-determined acceptable limits.

Primary responsibility for the management of risk lies with the business and operational areas responsible for the generation of risk exposure. Risk management provides an in-depth check against risk decisions and an ongoing platform to evaluate, monitor and sanction risk at the individual transaction and overall portfolio level.

Risk Management Structure

The Bank's risk management department reports directly to the Executive Risk Committee (a Board Committee).

The Bank's Risk Management includes the following four elements:

Risk Identification
↓
Risk Measurement
↓
Risk Monitoring
↓
Risk Control

Risk framework

The Bank has set up policies and measures to assess capital adequacy in terms of CBO regulations, which have been approved by the Board of Directors. Under these, the Bank assesses its capital against its risk profile, to ensure its capital is sufficient to support all material risks to which it is exposed.

The Board of Directors ensures that the senior management establishes a framework that identifies, measures, monitors and reports all relevant significant risks. The risk management department has identified material risks that the Bank is exposed to, and has defined the framework necessary to measure, monitor, and report these risks on a timely basis.

BASEL II PILLAR III AND BASEL III Report *(continued)*

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4. RISK EXPOSURE AND ASSESSMENT *(Continued)*

The following Board and Management committees manage and control material risks to the Bank:

Board Committees:

- Audit & Compliance Committee
- Executive & Credit Committee
- Executive Risk Committee
- Nomination & Remuneration Committee
- Head Office Project Committee

Management Committees:

- Credit & Investment Committee
- Assets & Liabilities Committee
- Credit Risk Management Committee
- Operational Risk Committee
- IT Steering Committee
- New Product Committee
- Special Assets Committee

The Bank's risk management is based on a 'Three Lines of Defense' model and is also supported by the fourth line of defense, to shield the Bank against risks that might threaten the achievement of its goals. This structure allows for a coordination of control responsibilities in an effective and efficient manner. To reach this objective, roles and responsibilities are clearly communicated to all the functions so that everyone understand his/her role and how it relates to the activities of other functions. Roles and responsibilities are communicated to the employees through policies and procedures and also through job descriptions. The following line of defenses are explained below:

First line of Defense

The business operations side which is the first line of defense is fully responsible for all the risks in its area of activity and has to ensure that effective controls are in place. In so doing, it ensures that the right controls are performed in the right way, that self-assessment of the business side is of a sufficiently high standard, that there is adequate awareness of risk and that sufficient priority/capacity is allocated to risk themes. The departments included in this line of defense are:

- Corporate Banking
- SME & Retail Banking
- Islamic Banking
- Treasury
- Information Technology
- Operations

Second Line of Defense

The Risk, Compliance, Finance and Legal Departments falls under the second line of defense. Independent of the business side, the second-line risk and control functions formulate their own opinion regarding the risks confronting the Bank. In this way, they provide an adequate degree of certainty that the first-line control function is keeping these risks under control, without taking over primary responsibility from the first line. In this regard, the second-line functions are tasked to identify, measure and report risks. The risk function has a veto right to ensure that it is respected.

The second-line risk and control functions also support the consistent implementation of the risk policy, the risk framework, etc., throughout the Bank, and supervise how they are applied. Compliance is an independent function that aims to prevent the Bank from being exposed to compliance risk or suffering harm through non-compliance with the prevailing laws, regulations or internal rules. It pays particular attention in this regard to compliance with the Integrity Policy.

Third Line of Defense

As the independent third-line of control, Internal Audit Department is responsible for the quality control of the existing business processes. It performs risk-based and general audits to ensure that the internal control and risk management system, including Risk Policy, are effective and efficient, and to ensure that policy measures and processes are in place and consistently applied within the Bank to guarantee the continuity of operations.

BASEL II PILLAR III AND BASEL III Report *(continued)*

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4. RISK EXPOSURE AND ASSESSMENT *(Continued)*

Fourth Line of Defense

Finally, there are additional external levels of controls that compliment three existing internal layers of control such as assurances from external independent bodies. External auditors are the common bodies under this line of defense. External auditors may not have the existing familiarity of the Bank that an internal audit department has, they can bring a new and valuable perspective. Accordingly they are important in the Bank's overall governance and control structure even though they are outsiders of the Bank.

Policies and Procedures:

The Board of Directors approve the Bank's risk appetite, risk management strategies, policies and the framework for their effective implementation and control, including delegated authorities to the Executive Committee and Management to approve all risk exposures. In this context, the Board of Directors has approved the following policies:

1. Anti-Money Laundering Manual
2. Personal Account Dealing Policy
3. New Product Policy and Procedures
4. Voice Recording Policy
5. Compliance Policy
6. Corporate Communication and Marketing policy
7. Corporate Governance Policy
8. Corporate Social Responsibility Policy
9. Dividend Policy
10. Expenses Policy
11. Capital Management Policy
12. Disclosure Policy
13. Board Remuneration Policy
14. Financial Institutions Policy
15. Human Resources Policy
16. Outsourcing Policy
17. Code of Business Conduct
18. Information Security Management Policy
19. Business Continuity Management Policy
20. Credit and Investment Policy
21. Operational Risk Management Framework
22. Operational Risk Management Policy
23. Fraud Risk Management Policy
24. . Fraud Risk Management Framework
25. Liquidity and Funding Policy
26. Market Risk Policy
27. Risk Management-Approach & Framework
28. Social and Environment Management System Policy
29. Security and Safety Policy and Plan
30. Asset Management Policy
31. Brokerage Policy
32. FATCA Policy
33. Customer Complaints Redressal Policy
34. Profit Distribution Policy
35. Charity Policy
36. Zakah Policy
37. Cost Sharing Policy
38. Segregation of Funds Policy
39. Social Media Policy
40. Shari'a Governance Manual
41. Electronic Banking Policy
42. Classification and Measurement Financial Assets and Liabilities
43. Sanctions Policy

All policies are subject to periodical reviews. Any change in law or regulation is deemed to be automatically adopted and implemented immediately upon its issuance (i.e. prior to the final amendment of the underlying policy or procedure).

BASEL II PILLAR III AND BASEL III Report *(continued)*

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The bank has exposure to the following risks:

5. CREDIT RISK

Qualitative Disclosure

Credit risk arises from the potential financial loss resulting from customers/counterparties failing to honor the terms of their contracts. It also includes the risk of loss in portfolio value as a result of migration from lower risk to higher risk categories. The Bank evaluates both settlement and pre-settlement credit risk at the customer level, across all products of the Bank.

Credit risk is the most significant risk incurred by the Bank, and proactive management is critical to the Bank's long-term success.

The Bank has a comprehensive due diligence system for approving credit facilities, and well defined policies on controlling credit risk at the counter-party, group, economic sector and country levels.

All corporate, bank and sovereign credit requires independent credit risk review to be approved by authorities, from Level II to the Board, depending on their delegated Credit Approval Jurisdiction (CAJ). All credit approvals are strictly in accordance with the regulatory guidelines issued from time to time by the CBO. Exceptions in retail credit exposure are escalated to Risk Management Department for necessary approvals.

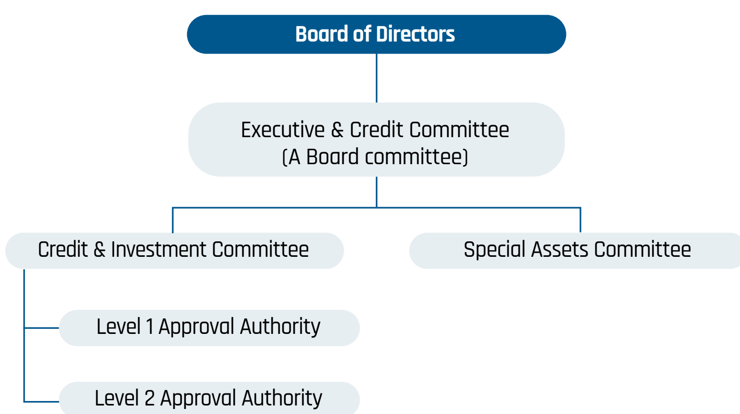
Risk Management quantifies the Bank's credit risk appetite in line with the Bank's strategic direction. A well-established process exists to ensuring the allocation of capital for the total credit risk to be assumed by the Bank; and measuring the actual use of capital at portfolio level.

With regard to credit culture, Risk Management ensures that the appropriate policies, guidelines, processes and procedures exist to cover all business areas of credit risk. It also ensures the consistent application of credit standards through a diligent Credit Review function and post approval review of loans through a Loan Review Mechanism (LRM) function and the periodic review and updating of credit policies, guidelines and procedures.

The Bank also has a robust system of borrowers' risk ratings that assesses the risk of corporate borrowers and monitors ratings changes periodically. In case of financial institutions, ratings by credit rating agencies are considered.

Structure and policies of credit risk management

The credit risk management policies are governed through Credit Risk Management Committee, Executive Risk Committee of the Board and the Board of Directors. The following is the structure of credit risk approval:-



The Bank has set up internal limits and approval authorities at various Management and Board Level Committees or the full Board based on the product category like Commercial Banking Lending, Country Limits or Limits for lending to Banks / FIs or Sovereigns and also lending related to the Bank's brokerage activities, the legal nature of the borrowers and their credit risk rating.

In regards to transaction risk, Risk Management ensures that credit is underwritten according to approved standards and that all risks are highlighted in the credit risk review, including policy exceptions. It includes analyzing and reporting on the nature of on-and off-balance sheet counter-party exposure (size, tenor, complexity and liquidity), including secured and unsecured credit facilities. To safeguard against concentration risk, sectoral limits have been set for ensuring that the Islamic window is having a well-diversified portfolio, the same is being reviewed by the Bank on a regular basis.

The Credit Risk Management Committee (CRMC) oversees, adherence to the limits, exceptions and makes recommendations to the Board in respect of policy related matters pertaining to credit risk management.

BASEL II PILLAR III AND BASEL III Report *(continued)*

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5. CREDIT RISK *(Continued)*

Past due credit exposures and Impairment policy

As a matter of policy, the Bank creates allowance for impairment of financing contracts promptly and in a consistent manner. The Bank has adopted IFRS 9 "Financial Instruments" accounting standard in 2018 based on which impairment is assessed on a forward looking expected credit loss (ECL) basis, as required by CBO.

The ECL Allowance is based on the credit losses expected to arise over the life of the asset (Lifetime ECL), unless there has been no significant increase in credit risk since origination, in which case, the allowance is based on 12 months expected credit loss (12 month ECL). The 12 month ECL is the portion of lifetime ECL that represent the ECLs that result from default events on a financial instrument that are possible within 12 months after the reporting date.

The Bank has established a policy to perform an assessment on a monthly basis 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 financing exposure into Stage 1, Stage 2 and Stage 3, as classified below:

Stage 1:

When Loans and advances & financing are first recognized, the Bank recognizes 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 Loans and advances & financing exposure has shown a significant increase in credit risk since origination, the Bank records an allowance for lifetime ECLs. Stage 2 financing exposure also include facilities, where the credit risk has improved and the financing exposure has been reclassified from stage 3.

Stage 3:

Loans and advances & financing exposure considered credit impaired. The Bank records an allowance for lifetime ECLs.

The Bank considers a financial asset to be in default when:

- the borrower is unlikely to pay its credit obligations to the Bank in full, without recourse by the Bank to actions such as realizing security (if any is held); or
- the borrower is past due more than 90 days on any material credit obligation of the Bank.
- in case of Treasury and interbank balances, when the required intraday payments are not settled by the close of business as outlined in the individual agreements.

Quantitative Disclosure:

i) Total gross credit risk exposures, plus average gross exposure over the period broken down by major types of credit exposure: (RO '000)

Sl. No.	Type of credit exposure	Average gross exposure		Total gross exposure	
		31-Dec-20	31-Dec-19	31-Dec-20	31-Dec-19
1	Overdrafts	75,423	72,957	74,369	76,477
2	Personal loans	738,865	699,668	749,488	728,241
3	Loans and against trust receipts	63,724	62,151	66,807	60,641
4	Other loans	1,288,824	1,141,437	1,365,948	1,211,698
5	Bills purchased/ discounted	20,172	24,593	20,885	19,458
	Total	**2,187,008**	**2,000,806**	**2,277,497**	**2,096,515**

BASEL II PILLAR III AND BASEL III Report *(continued)*

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5. CREDIT RISK *(Continued)*

ii) Geographic distribution of exposures by major type of credit exposure: (RO '000)

Sl No.	Type of Credit Exposure	Oman	Other GCC countries	OECD countries	India	Others	Total
1	Overdrafts	74,369	-	-	-	-	74,369
2	Personal loans	749,488	-	-	-	-	749,488
3	Loans against trust receipts	66,807	-	-	-	-	66,807
4	Other loans	1,349,181	848	15,082	441	396	1,365,948
5	Bills Purchased/discounted	20,885	-	-	-	-	20,885
6	Any	-	-	-	-	-	-
	Total	**2,260,730**	**848**	**15,082**	**441**	**396**	**2,277,497**

iii) Industry or counter party type distribution of exposures, broken down by major types of credit exposure: (RO '000)

Sl No.	Economic sector	Overdrafts	Loans	Bills purchased/ discounts	Others	Total	Off Balance Sheet Exposure
1	Wholesale and retail trade	9,179	135,698	3,610	84,412	232,899	50,903
2	Mining and quarrying	1,523	101,342	1,095	-	103,960	201
3	Construction	30,049	463,616	12,246	-	505,911	113,706
4	Manufacturing	11,921	111,883	2,235	-	126,039	14,921
5	Transport and communication	953	76,346	-	-	77,299	1,974
6	Electricity, gas and water	5,472	98,723	-	-	104,195	-
7	Financial institutions	198	161,212	72	-	161,482	3,693
8	Services	9,102	173,626	1,375	-	184,103	5,325
9	Personal loans	1,280	748,208	-	-	749,488	150
10	Non- resident lending	-	16,768	-	-	16,768	-
11	All	4,692	10,409	252	-	15,353	-
	Total	**74,369**	**2,097,831**	**20,885**	**84,412**	**2,277,497**	**190,873**

iv) Residual contractual maturity of the whole portfolio, broken down by major types of credit exposure: (RO'000)

Sl No	Time Band	Overdraft	Loans	Bills purchased/ discounted	Others	Total	Off Balance Sheet Exposure
1	Upto 1Month	3,718	146,205	9,071	-	158,994	98,078
2	1-3 Months	3,718	202,342	9,381	-	215,441	39,309
3	3-6 Months	3,718	109,835	2,433	-	115,986	35,147
4	6-9 Months	3,718	41,308	-	-	45,026	-
5	9-12 Months	3,718	46,890	-	-	50,608	9,713
6	1-3 Years	18,593	249,236	-	-	267,829	8,626
7	3-5 Years	18,593	205,496	-	-	224,089	-
8	Over5 Years	18,593	1,180,931	-	-	1,199,524	-
	Total	**74,369**	**2,182,243**	**20,885**	**-**	**2,277,497**	**190,873**

BASEL II PILLAR III AND BASEL III Report *(continued)*

31 December 2020

5. CREDIT RISK *(Continued)*

v) Major industry or counterparty type: (RO'000)

The Bank has set aside an additional amount of RO 0.998 million as a non-distributable special reserve on restructured loans based on CBO circular as at 31 December 2020.

Sl No	Economic sector	Gross loans	Of which Stage 3 exposure	Stage 1 & Stage 2 allowance^	Stage 3 allowance *	Impaiment allowance made during the year	Advances written off, net during the year
1	Wholesale & retail trade	232,900	15,036	1,979	13,809	14,176	-
2	Mining & quarrying	103,960	16	2,125	9	324	-
3	Construction	505,911	16,661	8,309	1,873	(77)	-
4	Manufacturing	126,039	5,251	1,736	1,423	1,277	-
5	Electricity, gas & water	104,195	-	215	-	79	-
6	Transport & communication	77,299	593	1,315	334	366	-
7	Financial institutions	161,482	-	1,319	-	385	-
8	Services	184,103	951	3,629	531	912	-
9	Personal loans	749,488	20,206	4,563	13,773	2,267	-
10	Non-resident lending	16,768	-	93	-	(2,678)	-
11	All others	15,352	7,688	1,523	42	40	-
	Total	**2,277,497**	**66,402**	**26,806**	**31,794**	**17,071**	**-**

*- Stage 3 allowance includes reserve interest amounting RO 5.268 million.

^- Stage 1&2 includes additional ECL overlays of RO 5.786 million and modification loss of RO 0.073 million

vi) Amount of impaired loans broken down by significant geographical areas including, with the amounts of impairment allowances related to each geographical area: (RO'000)

Sl No.	Countries	Gross loans	Of which Stage 3 exposure	Stage 1 & Stage 2 allowance^	Stage 3 allowance *	Impairment allowance made during the year	Advances written off, net during the year
1	Oman	2,260,730	60,530	26,761	29,097	17,101	-
2	Other GCC countries	848	-	1	-	(314)	-
3	OECD countries	15,082	5,431	39	2,431	268	-
4	India	441	441	-	266	29	-
5	Pakistan	-	-	-	-	-	-
6	Others	396	-	5	-	13	-
	Total	**2,277,497**	**66,402**	**26,806**	**31,794**	**17,071**	**-**

*- Stage 3 allowance includes reserve interest amounting to RO 5.268 million.

^- Stage 1&2 includes additional ECL overlays of RO 5.713 million and modification loss of RO 0.073 million

vii) Movement of gross loans: (RO '000)

SL No.	Details	Stage 1	Stage 2	Stage 3	Total
1	Opening balance	1,684,146	375,931	36,438	**2,096,515**
2	Mitigation/ changes (+/)	(69,839)	46,410	23,429	**-**
3	New loans	1,376,857	709,290	22,271	**2,108,418**
4	Recovery of loans	(1,221,993)	(689,707)	(15,698)	**(1,927,398)**
5	Loans written back	-	-	(38)	**(38)**
6	Closing balance	1,769,171	441,924	66,402	**2,277,497**
7	Impairment allowance held	8,315	18,491	26,526	**53,332**
8	Reserve interest	-	-	5,268	**5,268**

BASEL II PILLAR III AND BASEL III Report *(continued)*

31 December 2020

5. CREDIT RISK *(Continued)*

Credit risk- Disclosures for portfolios subject to the standardized approach.

As part of the standardized approach, the Bank follows the simplified approach for credit risk capital charge calculation. Accordingly, keeping in view the CBO guidelines, the Bank has used the financial collaterals such as cash, acceptable bank guarantees and shares listed on the MSM main index as part of the credit risk mitigation for arriving at the capital adequacy.

Qualitative Disclosures:

The Bank is following Moody's, S&P and Fitch rating for both sovereign and interbank exposures and the balance is treated as unrated at 100% risk. As per the guidelines, the ratings corresponding to the two lowest risk weights are considered and the higher of the two risk weights is applied. There has been no change in the approach compared to previous year.

The bank uses the discretion to treat loans and advances as unrated at risk weight of 100%, except housing loans and SME which are risk weighted at 35% and 75% based on the requirements as stipulated in the guidelines issued by CBO.

Similarly, the bank uses the discretion of the simple approach for recognizing collaterals.

Quantitative Disclosures:

Gross exposure amount as at 31 December 2020, subject to the standardized approach is as below:

RO 000's

S. No.	Product / Rating			Capital Charge				Total
		0%	20%	35%	50%	75%	100%	
	Rated							
1	Sovereign	344,033	-	-	-	-	824	**344,857**
2	Banks	-	19,868	-	27,717	-	9,722	**57,307**
	Unrated							
1	Corporate	-	-	-	-	137,850	1,170,752	**1,308,602**
2	Banks	-	3,200	-	15,400	-	-	**18,600**
3	Retail	-	-	-	-	-	447,024	**447,024**
4	Claims secured by residential property	-	-	53,322	-	-	221,391	**274,713**
5	Claims secured by commercial property	-	-	-	-	-	239,148	**239,148**
6	Past due loans	-	-	-	-	-	29,355	**29,355**
7	Other assets	14,594	-	-	-	-	114,517	**129,111**
	Total Banking Book	**358,627**	**23,068**	**53,322**	**43,117**	**137,850**	**2,232,733**	**2,848,717**

Credit Risk Mitigation: Disclosures for standardized approaches

Qualitative disclosure

Credit risk mitigation (CRM) encompasses collateral management and credit guarantee arrangements. The policies and processes for on-and off-balance sheet netting (and the extent to which the Bank makes use of them); policies and processes for collateral valuation and management; and a description of the main types of collateral taken are described below.

In respect of real estate collateral, two valuations are obtained if the value of collateral exceeds a particular level: the lowest valuation is used. The Bank also has a mandatory requirement to obtain an insurance policy on real estate collateral (other than land) where the policy is assigned in the Bank's favor. Real estate collateral is valued on regular intervals and also on need basis based on the assessment of risk and economic scenario prevailing.

BASEL II PILLAR III AND BASEL III Report *(continued)*

31 December 2020

5. CREDIT RISK *(Continued)*

The Bank normally accepts the following types of collateral:

- Cash margins and fixed deposits
- Real estate comprising income-producing and non-income-producing assets
- Shares listed on recognized stock exchanges located in GCC
- Irrevocable and unconditional guarantees / standby LC issued by acceptable Banks
- Debt securities subject to meeting approved criteria
- Funds subject to meeting approved criteria

The Bank also accepts guarantees of individuals and corporates to mitigate risks, wherever applicable and has a system of assessment of their creditworthiness.

Management monitors the market value of collateral at regular interval and requests additional collateral in accordance with the underlying agreement in case of shortfall. The Bank also periodically reviews the collateral cover for determining the adequacy of the allowance for impairment losses. The fair value of collateral that the Bank held as at 31 December 2020 towards loan and advances not impaired amounted to RO 1,859.559 million.

Quantitative disclosure

As per Basel & CBO guidelines the Bank stands in possession of the following eligible collateral:

1) Cash 2) Shares 3) Sovereign Guarantee.

Exposure covered by cash collateral – RO 3.237 million after application of haircut (0%) exposure stands at RO Nil.

Exposure covered by Shares collateral – RO 116.888 Million; after application of haircut (50%) exposure stands at RO. 58.444 Million.

Exposure covered by Sovereign guarantee RO 22.974 Million; after application of haircut (0%) exposure stands at RO Nil.

Particulars	RO 'Mn
Gross Exposure - banking book	2,849
Credit risk mitigation	(130)
Risk weight impact - for banking book	(448)
Risk weighted assets - banking book	2,270
Capital charge for credit risk	**278**

Counterparty Credit Risk:

Counterparty Credit Risk (CCR) is the risk that the customer or trading counterparty of the Bank, usually an OTC derivative contract, may fail to fulfill its obligation which may result in replacement or termination of transaction at a loss to the Bank.

Bank has implemented Current Exposure Method (CEM) for the measurement of Risk Weighted Assets under CCR. Exposure under CEM method is defined as sum of Potential Future Exposure (PFE) and Current Credit Exposure (CCE). The PFE is the estimate of amount of exposure that may occur over a one year time horizon while CCE is the sum of positive MTM (Mark to Market) values. Bank has total exposure (CEM) of OMR on account of OTC derivatives (FX forwards, Interest Rate Swaps etc) and RWA of RO 5.696 million as at 31 December 2020.

BASEL II PILLAR III AND BASEL III Report *(continued)*

31 December 2020

6. MARKET RISK

Qualitative disclosure

Substantially all of the Bank's businesses are subject to the risk that market prices and rates will move and result in profits or losses for the Bank. Market risk arises from fluctuations in interest rates, foreign exchange rates, commodity and equity prices. Market risk has been categorized into interest rate risk, equity position risk and foreign exchange risk. The Bank does not take any trading positions in commodities

The Bank has a robust Market Risk Management framework which comprises of risk identification, setting up of limits, monitoring, reporting, escalation matrix and resolution. The policy and procedure ensures that all limits are within risk appetite of the Bank and approved by the Board.

Details of various market risks are as below:

Interest Rate Risk Principles and Framework

Interest rate risk arises from the possibility that changes in interest rates will affect the value of underlying financial instruments. The Bank is exposed to interest 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 Bank's overall goal is to manage interest rate sensitivity so that movements in interest rates do not adversely affect the Bank's net interest income. Interest rate risk is measured as the potential volatility in net interest income caused by changes in market interest rates. The Bank manages this risk by matching or hedging the re-pricing profile of assets and liabilities through various risk management strategies.

Interest Rate Risk in Trading Book

Interest rate risk in the trading book is the risk of losses in the market value of underlying financial instruments and arises from the sensitivity of interest bearing instruments to interest rate volatility. Interest rate risk in the trading book is monitored through notional exposure limits, stop loss limits, and maximum maturity limits, and is marked to market.

As of 31 December 2020, there were no trading book position sensitive to interest rate changes.

Equity Position Risk

Equity position risk occurs due to change in market value of the Bank's equity portfolio due to change in general market or security specific conditions. The ALCO monitors all equity investment on periodic basis. The Market Risk and Mid Office is responsible to ensure appropriate risk limits are in place and reports the same to appropriate authorities.

As of 31 December 2020, equity investments classified as FVTPL amount to OMR 0.697 million.

Foreign Exchange Risk

Foreign exchange risk is the risk that the foreign currency positions taken by the Bank may be adversely affected due to volatility in foreign exchange rates. Foreign exchange risk management is ensured through regular measurement and monitoring of open foreign exchange positions. Treasury takes every possible measure to cover open positions created by customer transactions.

Instruments used to mitigate this risk are foreign exchange spot, forwards, deposits, etc. These instruments help to insulate the Bank against losses that may arise due to significant movements in foreign exchange rates. All foreign exchange exposures are centrally managed by the Bank's Treasury and are daily marked to market. Limits have been assigned with respect to overnight open exposures, stop loss and authorized currencies to monitor and control foreign exchange exposures.

The Bank treats its entire Foreign Exchange Exposure under Basel II Standardized method for capital calculation. The Net open position in all foreign currencies stands at RO 31.765 million (including RO 29.777 million open position is in effectively pegged currencies) as on 31 December 2020.

Quantitative Disclosure:

Capital Charge:

The exposure under the trading book of the Bank includes relatively small foreign exchange exposure primarily arising from the holding of day-end positions in currencies overnight, and exposure towards interest rate related instruments. Positons are monitored on daily basis to ensure open currency position is maintained within the regulatory limit. For the purpose of capital charge, the three month average of the sum of the net short positions or net long positions, whichever is higher, is taken. The average is worked out on the basis of the actual positions as obtained on all the working days during the three month period immediately preceding the reporting date.

In addition, the Bank holds insignificant FVTPL investments. The exposures are daily monitored by the Middle Office as per the approved stop loss and exposure limits.

BASEL II PILLAR III AND BASEL III Report *(continued)*

31 December 2020

6. MARKET RISK *(Continued)*

Table showing capital charge for interest rate, equity and FX risk as on 31 December 2020 is shown below:

Type of risk	2020	2019
Interest rate risk	-	-
Equity position risk	111	81
Foreign exchange risk	5,704	5,420
Percentage of NOP to regulatory capital	8.04%	20.16%
Regulatory ceiling (% to total networth)	40%	40%

Total risk weighted assets for trading book is RO 72.689 million with capital charge of RO 8.904 million.

Investments in the banking book

The Bank's investments will have to be within the overall limits and restrictions as CBO may prescribe from time to time.

However, the Bank has set up internal limits and approval authorities at various Management and Board Level Committees or the full Board of Directors based on the product category like Repo, CBO CD or Equity/Bonds, as a percentage of the Capital Base of the Bank. All investment proposals are routed through the ALCO to the relevant approval authority.

In addition to the CBO restrictions on investments by banks and such internal limits as described above, the following restrictions will apply:

The Bank's appetite for private subscriptions and unlisted/unquoted equity is low and any such proposals should be adequately justified on a case by case basis and has to be approved at least by the Executive & Credit Committee and by the Board if it exceeds limits structured as a proportion of the Bank's capital base.

All investments of the Bank should be in either USD or USD pegged GCC currencies or any investments in other currencies should be approved at least by the Executive & Credit Committee if it exceeds limits structured as a proportion of the Bank's capital base, after review and recommendation of the ALCO. Aggregate investments in all such currencies should not exceed a limit based on the Bank's capital base unless approved by the Board of Directors. This should include all investments through any Fund Manager, or proprietary investments made through the Bank's Asset Management Department.

Any investments of the Bank outside the GCC countries or US will have to be specifically approved by at least the Executive & Credit Committee if it exceeds limits structured as a proportion of the Bank's capital base. This should include all investments through any Fund Manager, or proprietary investments made through the Bank's Asset Management Department.

The Bank will try to achieve reasonable diversification of its equity investment portfolio among the economic sectors, and will not exceed a certain limit of its investment portfolio in any particular industry / sector groups listed below:

a. Trading and retailing

b. Real estate development, management and rental income

c. Construction / contracting and building materials

d. Travel / tourism, hotels, restaurants, entertainment, health services and education

e. Warehousing / storage, logistics, supply management and transportation, utilities and telecom

f. Oil and gas

g. Banking and financial services

h. Conglomerates or holding companies investing in any of the above business lines

This should include all proprietary investments made through the Bank's Asset Management Department.

Any proposal that leads to contravention of the above or any proposal for investment in any sector or industry not listed above will need approval of the Executive Credit Committee.

All investment approval requests for specific transactions or trading limits must be made by the relevant Business Line, approved by the Credit and Investment Committee and submitted to the Executive & Credit Committee as delegated. Any approval above those delegated limits is to be elevated to the Board level for approval. Any restrictions on investments as per effective CBO regulations shall apply. The details of investments are provided in Note 9 of the financial statements.

BASEL II PILLAR III AND BASEL III Report *(continued)*

31 December 2020

6. MARKET RISK *(Continued)*

Investment exits/ Stop loss (does not cover Asset Management Division operations)

Exit strategies is clearly outlined in all investment proposals. In case of a change in the exit strategy, approval from the same approving body is obtained. Sale of FVOCI investments to book profit is approved/ ratified by the ALCO.

The tolerance level of a decrease in the value of an FVTPL investment is a maximum of 15% (in a particular financial year). Investments exceeding this threshold are exited. Any holding with loss equivalent or greater than 10% (in a particular financial year) are notified to ALCO members. In case an investment is witnessing a material change (downgrading or expected downgrade, etc.), the Business Unit outlines the action/remedial plan for ALCO's review. Based on its review, ALCO decides the most appropriate strategy and notify the Credit and Investment Committee.

Interest Rate Risk in Banking Book (IRRBB)

The Bank monitors its interest rate risk in the banking book through performing repricing gap analysis of interest rate sensitive assets and liabilities. Under repricing gap analysis, the Bank distributes interest rate sensitive assets and liabilities into time bands according to their maturity (if fixed rate) or time remaining to their next repricing (if floating rate). The size of the gap for a given time period – that is assets minus liabilities that reprice or mature within that time band – gives an indication of the Bank's repricing risk exposure. The Bank evaluates the effect of a parallel shift in yield curve on its economic value by applying a proxy for modified duration multiplied by the assumed parallel change in interest rates to the gap under each time band.

The nature of IRRBB and key assumptions, including assumptions regarding loan prepayments and behavior of non-maturity deposits, and frequency of IRRBB measurement, are given below.

Interest rate risk is mainly related to retail banking book as they are re-priced with any change in the CBO's interest rate and for corporate customer re-priced in line with the market conditions.

Deposits are re-priced based on their final maturity, or if linked to a floating rate index, on the re-pricing date. Deposits that are insensitive to interest rate movements are categorized separately. The earnings at risk are calculated based on interest rate re-pricing gaps. The Bank is confident of sourcing the cheaper source of funds by way of customers' deposits. ALCO along with the risk management department identifies interest rate risk and these are monitored and reported periodically. Rate sensitive exposures are quantified using re-pricing gaps.

Quantitative Disclosure:

Exposure and sensitivity analysis

The sensitivity of interest rate risk is determined by applying 200 bps interest rate shock on net interest income and assessing the impact on capital. The impact of a 200 basis points parallel shift in interest rate is provided below:

	2020	2019
	RO '000	RO '000
Impact of +200 bps interest rate increase	**7,768**	7,487
Impact of -200 bps interest rate decrease	**(7,768)**	(7,487)
Impact of +200 bps interest rate increase as % of Capital	**+1.97%**	+1.98%
Impact of -200 bps interest rate decrease as % of Capital	**-1.97%**	-1.98%

The bank's interest sensitivity position, in line with guidelines issued by Central bank of Oman, based on contractual re-pricing arrangements at 31 December 2020 is highlighted in Note 37.3.2 of the financial statements.

BASEL II PILLAR III AND BASEL III Report *(continued)*

31 December 2020

7. LIQUIDITY RISK

Qualitative Disclosure

The Bank defines liquidity risk as its ability to meet all present and future financial obligations in a timely manner and without undue effort and cost through unconstrained access to funding at reasonable market rates and without affecting asset growth and business operations.

The following key factors are taken into consideration while assessing and managing the liquidity risk of the Bank:

- The need to have a well-diversified base for funding sources, comprising a portfolio of retail customers, large corporates and institutions, small & medium enterprises, high net worth individuals, without significant concentrations or correlations, thereby diversifying the funding base and mitigating concentration risks.
- Based upon the past behavioral pattern analysis of our main liabilities, management expects large portion of customer deposits to be rolled over at contractual maturity.
- As per the CBO directives, the Bank keeps at least 5% of its demand & time deposit liabilities with CBO in the form of clearing balances
- Commitments for loans and advances are approved after taking into account the Bank's overall liquidity position.

The Bank's projected liquidity needs are analyzed and optimum alternatives to manage the liquidity risk are discussed and approved in ALCO. The Risk Management department also independently reviews and evaluates the Bank's ability to access liquidity from different sources.

The Treasury and Risk management Departments identify liquidity at risk, which is monitored daily and reported periodically to ALCO. Liquidity and Funding Policy and a liquidity contingency plan have been established by the Bank.

Liquidity and Funding Policy

The Liquidity and Funding policy of the Bank is intended to ensure that liquidity requirements are prudently and effectively managed such that anticipated and unanticipated funding needs are met on an ongoing basis in a controlled manner at the least possible cost.

The Bank's ALCO reviews the Liquidity Policy annually and submits recommendations for changes, if any, to the Bank's Chief Executive Officer (CEO) for review and submission to the Executive Committee and Board as applicable.

There are a number of techniques which the Bank uses to manage its Liquidity position. The key ones are:

- Placing limits on maturity mismatches
- Maintaining a stock of liquid assets
- Diversification of liabilities
- Access to wholesale markets
- Multi-currency liquidity management

The Bank also maintains significant investments in liquid instruments issued by Government & banks principally for maintaining liquidity. The Bank also has standby lines of credit to meet its obligations at any given time, if the need arises.

Stock of Liquid Assets

An adequate stock of high quality liquid assets provides the Bank with the capacity to meet its obligations while any underlying problems affecting liquidity are addressed.

Such assets are clearly identified, their role defined and minimum holding levels are established and agreed by the ALCO. The degree of diversification of the liquid assets portfolio is reviewed by the ALCO on a monthly basis.

As per the guidelines of CBO, the Bank is required to maintain Liquidity Coverage Ratio (LCR) of at least 100%. Further, Net Stable Funding Ratio (NSFR) is also prescribed at a minimum of 100%. Internally, the Bank has implemented a more stringent requirement for these ratios which is reviewed by ALCO on a monthly basis. A detailed disclosure on the position of the Bank in regards to these ratios is contained later in this report.

Diversification of liabilities

The Bank seeks to maintain a diversified funding base, and monitors the degree of diversification in its liability base on a monthly basis. Depositor concentration is reviewed by the ALCO on a monthly basis.

The liquidity policy recognizes the inherent value of the Bank's longer term depositors. The Bank seeks to establish strong and lasting relationships with depositors and other liability holders so as to foster a stable funding base. Trends in liability balances by category are reviewed by the ALCO on a monthly basis.

BASEL II PILLAR III AND BASEL III Report *(continued)*

31 December 2020

7. LIQUIDITY RISK *(Continued)*

The Bank also recognizes that an over reliance on short dated inter-bank deposits can lead to difficulties in extreme market conditions. The Bank's exposure to such deposits is reviewed by the ALCO on a monthly basis.

Multi-currency liquidity

Where positions in specific foreign currencies are significant to its business, the Bank addresses the measurement and management of liquidity in these individual currencies. It is considered appropriate to consolidate several (usually minor) currencies and monitor the aggregate exposure expressed in base currency.

When monitoring exposure in aggregate, the Bank assesses the convertibility of individual currencies, the timing of access to funds, the impact of potential disruptions to foreign exchange markets and exchange risks before presuming that surplus liquidity in one currency can be used to meet a shortfall in another currency.

Performance against limits is monitored daily by Treasury with any exceptions being immediately reported to ALCO members. Review of all liquidity positions against limits is performed by Head of Risk Management and Treasury based on figures produced by the Treasury Middle Office / Finance Department.

The Treasurer along with the Head of Risk Management derives and documents the Maturity Profile behavioral adjustments, based on redemptions and withdrawal requests. These are communicated to the ALCO for discussion and acceptance.

Liquidity Contingency Plan:

It is imperative for the Bank to maintain an adequate amount of liquid assets as a protection against a possible loss in the event of emergency situation. The Bank's Liquidity Contingency Plan (LCP) is approved by Board and addresses the institution's strategy for handling any liquidity crisis. LCP will serve as the blueprint for meeting its funding needs under stress environment in a timely manner and at a reasonable cost. It describes policies and procedures for managing or making up cash flow shortfalls in such situations at both solo and consolidated level.

The Bank has adopted quantitative and qualitative key warning indicators which is monitored by Market Risk team and presented to ALCO. The members of the Liquidity Crisis Management Team (LCMT) and ALCO are notified immediately should any of the early warning criteria be breached.

In the event of the plan being invoked, ALCO delegates the responsibility for the management of the Bank's liquidity to the LCMT. The LCMT is comprised of CEO (Chairman), DCEO Wholesale Banking , DCEO – Support Services, Head of Finance, Head of Treasury and Head of Risk.

Quantitative disclosure

The maturity gaps are measured and reported as per CBO circular BM 955 dated May 7, 2003 and subsequent amendments including the CBO circular dated March 20, 2018 on Maturity of Assets and Liabilities. Disclosure pertaining to the maturity profile of assets and liabilities as at 31 December 2020 are provided in note 37.2.2 of financial statements. Following is the position of currency-wise cumulative gaps as % of cumulative liabilities as monitored against CBO prescribed maximum limits:

as of 31 December 2020

Currency	Upto 1 month	1 - 3 months	3 - 6 months	6 - 9 months	9 - 12 months
Aggregate	47.7%	29.0%	21.3%	-0.7%	-12.8%
OMR	40.6%	51.6%	37.1%	2.1%	-12.0%
USD	56.2%	-12.7%	-11.6%	-10.6%	-17.0%
Others	142.3%	103.3%	56.8%	52.7%	41.1%

as of 31 December 2019

Currency	Upto 1 month	1 - 3 months	3 - 6 months	6 - 9 months	9 - 12 months
Aggregate	33.2%	18.8%	9.6%	-1.3%	-21.3%
OMR	47.0%	32.0%	19.4%	2.1%	-22.9%
USD	16.1%	-0.3%	-8.0%	-10.4%	-22.4%
Others	38.9%	13.7%	11.6%	10.2%	7.7%
CBO prescribed Limits	-15%	-15%	-20%	-25%	-25%

BASEL II PILLAR III AND BASEL III Report *(continued)*

31 December 2020

8. OPERATIONAL RISK

Operational Risk Framework

Operational risk is the risk of direct or indirect loss resulting from inadequate or failed internal processes, people, and systems or from external events.

Losses from external events such as a natural disaster that has a potential to damage the Bank's physical assets or electrical or telecommunication failures that disrupt business are relatively easier to define than losses from internal problems such as employee fraud and product flaws. The risks from internal problems are more closely tied to the Bank's specific products and business lines; they are more specific to the Bank's operations than the risks due to external events. Operational risks faced by the Bank include IT Security, telecom failure, frauds and operational errors.

Operational risk is controlled through a series of strong internal controls and audits, well-defined segregation of duties and reporting lines, operational manuals and standards. Internal audit independently reviews the effectiveness of the Bank's internal controls and its ability to minimize the impact of operational risks. The Bank has an Operational Risk Management Framework elucidating the processes involved in the operational risk management. There is an Operational Risk Committee that is the owner of this Framework and holds responsibility.

The Bank identifies and assesses the operational risk inherent in its key material products, activities, processes and systems. It also ensures that before any new products or services, activities, processes or systems are introduced; the associated operational risks are properly assessed and mitigated.

Risk identification is vital to the development of operational risk monitoring and control systems. Risk identification considers internal factors such as the Bank's structure, the nature of its activities, the quality of its human resources, organizational changes, and employee turnover. It also examines external factors such as changes in the industry, major political and economic changes and technological advances.

The Bank has identified the following operational risks and has been implementing an effective framework to manage them:

- Fraud Risk
- Process Risk
- Legal Risk
- People Risk
- Compliance Risk
- IT Risk
- Physical Security Risk

In order to effectively manage the risks arising from frauds, in line with the CBO Circular on Fraud Risk Management, the Bank has introduced separate Fraud Risk Management (FRM) Policy and FRM Process. The FRM unit forms part of the Operational risk management division of Risk Management functions and is independent of other departments.

Control and Mitigation of Operational Risk

The Bank has established policies, processes and procedures to control and mitigate material operational risks. It periodically reviews risk limitation and control strategies and adjusts the operational risk profile accordingly, using appropriate strategies in light of its overall risk appetite and profile.

Towards this, the Bank has implemented Operation Risk Self-Assessment (ORSA) procedure for each of its business segments, where operating risk related to each business area is identified; documented and corresponding control processes are defined and documented. The action points arising from ORSA are reviewed and reported at the Operational Risk Committee on a regular basis. The Bank also has Key Risk Indicators (KRIs) in place and monitors these on a regular basis.

The Bank ensures that there is appropriate segregation of duties and personnel are not assigned responsibilities that may create a conflict of interest or enable them to conceal losses, errors or inappropriate actions.

The Bank ensures adequate internal audit coverage to verify that operating policies and procedures have been implemented effectively.

The Bank takes insurance cover to mitigate operational risk, wherever applicable.

It also ensures that internal practices exist to control operational risk such as:

- Maintaining safeguards for access to, and use of, the Bank's assets and records;
- Ensuring staff have appropriate expertise and training;
- Regularly verifying and reconciling transactions and accounts.

BASEL II PILLAR III AND BASEL III Report *(continued)*

31 December 2020

8. OPERATIONAL RISK *(Continued)*

Reputation Risk

Reputation Risk is negative public opinion/reaction which could cause damage to the Bank's profitability or image. Reputation risk is one of the most complex risks to manage in view of unpredictability, constant change in the operating environment, personnel turnover and multi-cultural environment that the Bank operates in. The Bank identifies, measures, monitors and controls reputation risk arising in the following areas:

- Customer service
- Perception of stakeholders regarding Bank's commitment to their interests
- Quality of products, services and sales practices
- Reporting to stakeholders and external agencies
- Accuracy of information in communications to the public

There are policies and procedures in place to manage and monitor reputation risk.

Social Media risk is an important element of Reputation risk that has emerged with the popularity of social media and digital technologies. The Bank recognizes the importance of effectively managing the interests of the Bank and its customers from this dynamic and unregulated category of risk. The Corporate Communication Department (CCD) is responsible for managing the Bank's social media activities within the guidelines of 'Social Media Policy'.

Business Continuity Risk

The Bank has documented the Business Continuity Management Policy (BCP) which outlines the business continuity process to be followed in a disaster scenario and undertakes comprehensive testing of all its critical systems and processes. The BCP aims to minimize the severity and impact of a disaster while continuing to serve both the business and customers with a lowest achievable detriment in service. The plan considers the following:

- Disaster scenarios and magnitude
- Various steps to mitigate the risk
- Impact on the Bank's business and operations
- The resources required for resuming the operations at the earliest possible time following the disaster
- Operating processes and available systems at the Disaster Recover (DR) site

Business Continuity Test

During the year 2020, the Bank has carried out a comprehensive BCP test and a volume test on a working day in order to test the resilience of the Bank's business systems at the DR site. The scope of the test was arrived at based on the Business Impact Analysis (BIA) carried by the Bank and the results of the BCP/ volume tests were submitted to the Board. The Bank has in place a crisis management team and the processes to be followed during a disaster scenario has been detailed out in the BCP documents of the Bank.

Fraud Risk Management

The Bank takes effective prevention and detection of fraudulent activities extremely serious and cooperate with the judicial and regulatory authorities and support national, regional and international initiatives to combat fraud. It endeavors to develop a culture of fraud awareness and prevention across all areas of its operations to limit possible financial losses and safeguard the brand and financial reputation of the Bank.

Concentration Risk

Concentration risk arises from exposure to a common set of factors that can produce losses large enough to threaten the Bank's health or ability to maintain its core business. Concentration risk can arise from large exposure to counterparty, a sector or country. Concentration risk can be mitigated by formulating limits, by a thorough check on counterparty's quality or adequate collateral support etc.

As part of ICAAP, thresholds for exposure concentrations has been set up, this will trigger additional capital requirements based on concentration in terms of large exposures to counterparties, sector exposure concentration (excluding retail lending) and geographical exposure concentration (other than to Oman).

BASEL II PILLAR III AND BASEL III Report *(continued)*

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8. OPERATIONAL RISK *(Continued)*

Information Security Risk

The bank has adopted an Information Security Management System (ISMS) /process and a framework by which the Bank ensures, protects and secures information resources that process and maintain information which are vital to its operations. The main component of this framework is the Information Security Policy that provides direction for formulation, implementation, and management of Information Security Management System. Since protection of customer information is the top-most priority, the Bank strives to safeguard the confidentiality, availability and integrity of the data of its customers and business partners at all times.

Compliance Risk (including risk of Shari'a Non-Compliance)

Compliance risk is the potential for financial losses, legal penalties, regulatory sanctions and loss to Bank's reputation that result from non-compliance with laws and regulations that are applicable to the Bank. The Board of Directors have direct responsibility for overseeing the management of the Bank's compliance risk. Senior management are thereafter responsible for ensuring effective management of this risk. They are supported by the Compliance function of the Bank which is an independent function that reports and has direct access to Board Audit & Compliance Committee. The Bank's 'Compliance Policy' sets the guidelines to manage this important risk type.

Shari'a Governance framework ensures Shari'a compliance at all times and at all levels. Shari'a compliance unit facilitates the senior management in ensuring compliance with Shari'a and Islamic banking stipulations of the Central Bank in all its business activities, operations and transactions. Shari'a compliance unit is extensively involved before a new product or transaction is approved and monitors the implementation of guidelines issued by Shari'a Supervisory Board (SSB). No new product class or transaction type is executed without consulting the Shari'a compliance unit and getting a formal approval from the SSB.

Model Risk

Model risk is the potential for ineffective decision making or regulatory non-compliance resulting from the use of insufficiently accurate models, particularly in the areas such as measuring, pricing and managing risks. These models include, but are not limited to, capital calculation model, facility and obligor risk rating models, models to calculate expected credit losses and provisioning, pricing models for investments and hedges etc. The Bank manages this risk by following best-practices in regards to governance, data management, model validation and back-testing of its key models.

Other Risks

The Bank is also exposed to other risks such as, strategic risk, business cycle risk, legal risk, residual risk, settlement risk, Shariah non- compliance risk (Pertaining to Islamic Banking) etc. However, currently these risks are not significant to the Bank. The Bank follows standard methodologies for arriving at the capital adequacy requirements of these risks. These risks are assessed and such assessments form part of the Bank's ICAAP process.

Operational risk capital charge and risk weighted amount

The Bank follows basic indicator approach for determining operational risk. The Capital charge for operational risk under Basic Indicator approach is calculated by taking the average of gross income multiplied by 15%, for each of the last three financial years, excluding years of negative or zero gross income. The gross income is Net interest income (+) Non interest income (+) Provisions for unpaid interest (-/+) gain/ loss on sale of investments (-) extraordinary / irregular items of income.

Item (RO '000)	**2020**	**2019**	**2018**
Net interest income	60,094	57,039	52,054
Non-interest income	11,402	12,710	10,099
Provision for unpaid interest	2,391	747	970
Gain on sale of investment	12	-	-
Insurance and other irregular items	(2)	(30)	(61)
Gross income	**73,897**	**70,466**	**63,062**

Average Income	69,142
Gross Income times of Alpha (15%)	10,371
Operational risk based on Basic Indicator Approach	129,637

Capital Charge for Operational Risk under Basic Indicator Approach as per Basel II is RO 9.396 million as of 31 December 2020.

The Risk weighted assets for operational risk as per Basel II is RO 117.449 million with the capital charge of RO 14.387 million.

BASEL II PILLAR III AND BASEL III Report *(continued)*

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9. COMPENSATION POLICY

In line with the CBO guidelines on remuneration disclosures as part of Pillar III, the Bank is committed to fair, balanced, performance-oriented compensation practices that align long-term employee and shareholder interests. The policy is endeavored to attract, retain and motivate the best people in the industry. The Bank has a Board appointed Nomination and Remuneration Committee whose primary objective is to advise the Bank's Board Chairman on the remuneration of Board members, appointment and remuneration of senior management personnel.

Performance awards are based on the achievement of both financial and non-financial objectives. The Performance Management System is aimed at achieving the Bank's business plans and objective through continuous and focused performance of the employees. The Objective of Performance Review process is to assess the employee on his/her performance against assigned Key Performance Indicators and Objectives. At senior management levels, the overall Bank's performance is the overriding criteria while awarding performance awards. The payout is based on consideration of all aspects governing performance including the stage of business, market conditions, and time horizon of risks, sustainable returns and the cyclical nature of certain businesses. The Bank is committed to responsible compensation practices which balance reward based on performance and promoting principled behavior and actions. The compensation is designed to contribute to the Bank's objectives and encourages prudent risk taking and adherence to applicable laws, guidelines and regulations.

The compensation policy and arrangement for Senior Management, Material Risk takers and Control functions in regulated roles of the Bank are based on their responsibilities and authority levels and are governed by the instructions from CBO on the principles and standards of the Financial Stability Board and relevant CMA regulations.

The list of Senior Management and Material Risk Takers in regulated roles of the Bank is reviewed annually by the Board Nomination and Remuneration Committee (NRC) and takes into account changes in terms of internal organization and compensation levels.

The NRC review and approves all fixed and variable compensation including all benefits for the designated Senior Management and Material Risk Takers in regulated roles of the Bank to ensure that payments made are fair to the individual and the Bank, that failure is not rewarded and that the duty to maximize performance and mitigate loss is fully recognized.

In cases whereby the variable compensation for Senior Management and Material Risk Takers exceeds threshold, the balance is being deferred and paid equally over the period of 3 years, subject to certain conditions relating to Malus and Claw-back criterion.

The key management comprises of 5 members (2019: 5 members) of the management committee.

The below table provides details of key management compensation:

	2020	2019
	RO '000	RO '000
Salaries and allowances	**1,127**	974
End of service benefits	**19**	30
Total	**1,146**	1,004

10. SUBSIDIARIES AND SIGNIFICANT INVESTMENTS

The Bank does not have any subsidiary or other significant equity investments as on 31 December 2020.

BASEL II PILLAR III AND BASEL III Report *(continued)*

31 December 2020

11. BASEL III CAPITAL DISCLOSURE

The below capital disclosures are prepared in accordance with the requirements of the CBO Circular BM 1114 'Regulatory Capital and Composition of Capital Disclosure Requirements under Basel III' issued on 17 November 2013.

11.1 The 3 step approach to reconciliation

Below disclosures are prepared using three step reconciliation approach as defined in the CP2-Guidelines on composition of capital disclosure requirements issued along with the CBO Circular BM 1114.

BASEL III COMMON DISCLOSURE TEMPLATE

	Common Equity Tier 1 capital: instruments and reserves	RO(000's)
1	Directly issued qualifying common share capital () plus related stock surplus/premium	164,966
2	Retained earnings (net of proposed cash dividend of 5%)	37,149
3	Accumulated other comprehensive income (and other reserves)	45,428
4	Directly issued capital subject to phase out from CET1 (only applicable to non-joint stock companies)	-
5	Common share capital issued by subsidiaries and held by third parties (amount allowed in group CET1)	-
6	**Common Equity Tier 1 capital before regulatory adjustments**	**247,543**
	Common Equity Tier 1 capital: regulatory adjustments	
7	Prudential valuation adjustments	(5,008)
8	Goodwill (net of related tax liability)	-
9	Other intangibles other than mortgage-servicing rights (net of related tax liability)	(3,491)
10	Deferred tax assets that rely on future profitability excluding those arising from temporary differences (net of related tax liability)	-
11	Cash-flow hedge reserve	-
12	Shortfall of provisions to expected losses	-
13	Securitization gain on sale (as set out in paragraph 14.9 of CP-1)	
14	Gains and losses due to changes in own credit risk on fair valued liabilities	-
15	Defined-benefit pension fund net assets	-
16	Investments in own shares (if not already netted off paid-in capital on reported balance sheet)	-
17	Reciprocal cross-holdings in common equity	-
18	Investments in the capital of banking, financial, insurance and takaful entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than the issued share capital (amount above 10% threshold)	-
19	Significant investments in the common stock of banking, financial ,insurance and takaful entities that are outside the scope of regulatory consolidation, net of eligible short positions (amount above 10% threshold)	-
20	Mortgage servicing rights(amount above 10% threshold)	-
21	Deferred tax assets arising from temporary differences (amount above 10% threshold, net of related tax liability)	-
22	Amount exceeding the 15% threshold	-
23	of which: significant investments in the common stock of financials	-
24	of which: mortgage servicing rights	-
25	of which: deferred tax assets arising from temporary differences	-
26	National specific regulatory adjustments	-
27	Regulatory adjustments applied to Common Equity Tier 1 due to insufficient Additional Tier 1 and Tier 2 to cover deductions	-
28	**Total regulatory adjustments to Common equity Tier 1**	**(8,499)**
29	**Common Equity Tier 1 capital (CET1)**	**239,044**

BASEL II PILLAR III AND BASEL III Report *(continued)*

31 December 2020

11. BASEL III CAPITAL DISCLOSURE *(Continued)*

11.1 The 3 step approach to reconciliation *(Continued)*

	Additional Tier 1 capital: Instruments	
30	Directly issued qualifying Additional Tier 1 instruments plus related stock surplus (31+32)	124,000
31	of which: classified as equity under applicable accounting standards	124,000
32	of which: classified as liabilities under applicable accounting standards	-
33	Directly issued capital instruments subject to phase out from Additional Tier 1	-
34	Additional Tier 1 instruments (and CET1 instruments not included in row 5) issued by subsidiaries and held by third parties (amount allowed in group AT1)	-
35	of which: instruments issued by subsidiaries subject to phase out	-
36	**Additional Tier 1 capital before regulatory adjustments**	**124,000**
	Additional Tier 1 capital : regulatory adjustments	
37	Investments in own Additional Tier 1 instruments	-
38	Reciprocal cross-holdings in Additional Tier 1 instruments	-
39	Investments in the capital of banking, financial, insurance and takaful entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued common share capital of the entity (amount above 10% threshold)	-
40	Significant investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation (net of eligible short positions)	-
41	National specific regulatory adjustments	-
	OF WHICH: [INSERT NAME OF ADJUSTMENT]	-
	OF WHICH:	-
42	Regulatory adjustments applied to Additional Tier 1 due to insufficient Tier 2 to cover deductions	-
43	**Total regulatory adjustments to Additional Tier 1 capital**	**-**
44	**Additional Tier 1 capital (AT1)**	**124,000**
45	**Tier 1 capital (T1 = CET1 + AT1)**	**363,044**
	Tier 2 capital: instruments and provisions	
46	Directly issued qualifying Tier 2 instruments plus related stock surplus	
47	Directly issued capital instruments subject to phase out from Tier 2	600
48	Tier 2 instruments (and CET1 and AT1 instruments not included in rows 5 or 34) issued by subsidiaries and held by third parties (amount allowed in group Tier 2)	
49	of which: instruments issued by subsidiaries subject to phase out	
50	Provisions (including gain on investments)	21,848
51	**Tier 2 capital before regulatory adjustments**	**22,448**
	Tier 2 capital: regulatory adjustments	
52	Investments in own Tier 2 instruments	-
53	Reciprocal cross-holdings in Tier 2 instruments	-
54	Investments in the capital of banking, financial, insurance and takaful entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued common share capital of the entity (amount above the 10% threshold)	-
55	Significant investments in the capital banking, financial and insurance entities that are outside the scope of regulatory consolidation (net of eligible short positions)	-
56	Total National specific regulatory adjustments	-
	Of which: Investments in Tier 2 capital of unconsolidated banking and financial subsidiary companies, associates or affiliates etc.,	-
	Of which: shortfall in the Tier 2 regulatory capital in the unconsolidated entities	-

BASEL II PILLAR III AND BASEL III Report *(continued)*

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11. BASEL III CAPITAL DISCLOSURE *(Continued)*

11.1 The 3 step approach to reconciliation *(Continued)*

57	**Total regulatory adjustments to Tier 2 capital**	**-**
58	**Tier 2 capital (T2)**	**22,448**
59	**Total capital (TC = T1 + T2)**	**385,492**
60	**Total risk weighted assets**	**2,460,452**
60a	Credit risk weighted assets	2,270,314
60b	: Market risk weighted assets	72,689
60c	: Operational risk weighted assets	117,449
	Capital Ratios and buffers	
61	Common Equity Tier 1 (as a percentage of risk weighted assets)	9.72%
62	Tier 1 (as a percentage of risk weighted assets)	14.76%
63	Total capital (as a percentage of risk weighted assets)	15.67%
64	Institution specific buffer requirement (minimum CET1 requirement plus capital conservation buffer plus countercyclical buffer requirements plus G-SIB buffer requirement expressed as a percentage of risk weighted assets)	8.250%
65	of which: capital conservation buffer requirement	1.250%
66	of which: bank specific countercyclical buffer requirement	-
67	of which: G-SIB buffer requirement	-
68	Common Equity Tier 1 available to meet buffers (as a percentage of risk weighted assets	2.72%
	National Minima (if difference from Basel 3)	
69	National Common Equity Tier 1 minimum ratio (if different from Basel 3 minimum)	8.250%
70	National Tier 1 minimum ratio (if different from Basel 3 minimum)	10.250%
71	National total capital minimum ratio (if different from Basel 3 minimum)	12.250%
	Amounts below the thresholds for deduction (before risk weighting)	
72	Non-significant investments in the capital of other financials	771
73	Significant investments in the common stock of financials	
74	Mortgage servicing rights (net of related tax liability)	-
75	Deferred tax assets arising from temporary differences (net of related tax liability)	-
76	Provisions eligible for inclusion in Tier 2 in respect of exposures subject to standardised approach (prior to application of cap)	19,129
77	Cap on inclusion of provisions in Tier 2 under standardised approach	20,715
78	Provisions eligible for inclusion in Tier 2 in respect of exposures subject to internal ratings-based approach (prior to application of cap)	-
79	Cap for inclusion of provisions in Tier 2 under internal ratings-based approach	-
	Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2018 and 1 Jan 2022)	
80	Current cap on CET1 instruments subject to phase out arrangements	-
81	Amount excluded from CET1 due to cap (excess over cap after redemptions and maturities)	-
82	Current cap on AT1 instruments subject to phase out arrangements	-
83	Amount excluded from AT1 due to cap (excess over cap after redemptions and maturities)	-
84	Current cap on T2 instruments subject to phase out arrangements	-
85	Amount excluded from T2 due to cap (excess over cap after redemptions and maturities)	-

BASEL II PILLAR III AND BASEL III Report *(continued)*

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11. BASEL III CAPITAL DISCLOSURE *(Continued)*

11.1 The 3 step approach to reconciliation *(Continued)*

Step 1: Balance sheet under Regulatory scope of consolidation

Table 2a- Balance sheet under Regulatory Scope of Consolidation (RO '000)

Year ended 31 December 2020	Published financial statements	Under regulatory scope of consolidation
Assets		
Cash and balances with Central Bank of Oman	79,020	79,020
Certificates of deposit	-	-
Due from banks	46,174	46,174
Loans and advances	2,218,897	2,218,897
Investments in securities	306,368	306,368
Loans and advances to banks	-	-
Property and equipment	22,864	22,864
Deferred tax assets	-	-
Other assets	29,154	29,154
Total assets	**2,702,477**	**2,702,477**
Liabilities		
Due to banks	135,244	135,244
Customer deposits	1,924,654	1,924,654
Borrowings	159,775	159,775
Deferred tax liabilities	286	286
Other liabilities	82,168	82,168
Subordinated bonds	12,000	12,000
Total liabilities	**2,314,127**	**2,314,127**
Shareholders' Equity		
Paid-up share capital	164,966	164,966
Share premium	-	-
Legal reserve	34,028	34,028
General loan loss reserve	-	-
Impairment reserve	10,127	10,127
Retained earnings	46,897	46,897
Special reserve	998	998
Cumulative changes in fair value of investments	(4,066)	(4,066)
Subordinated debt reserve	11,400	11,400
Total shareholders' equity	**264,350**	**264,350**
Tier 1 Perpetual subordinated bonds	124,000	124,000
Total equity	**388,350**	**388,350**
Total liability and shareholders' funds	**2,702,477**	**2,702,477**

BASEL II PILLAR III AND BASEL III Report *(continued)*

31 December 2020

11. BASEL III CAPITAL DISCLOSURE *(Continued)*

11.1 The 3 step approach to reconciliation *(Continued)*

Step 2: Expansion of Balance sheet under Regulatory scope of consolidation

Table 2b – Expansion of Balance Sheet Under Regulatory Scope of Consolidation (RO '000)

For the year ended 31 December 2020	2020 financial Statement	Under Regulatory scope of consolidation	Reference
Assets			
Cash and balances with CBO	**79,020**	**79,020**	
Balance with banks and money at call & short notice	**46,174**	**46,174**	
Balance with banks and money at call & short notice, of which:		**46,298**	
- Stage1 / 2 impairment allowance , of which	-	(124)	
- amount eligible for T2	-	-	
Investments, of which:	**306,368**	**306,368**	
Fair Value Through Other Comprehensive income (FVOCI)	-	305,671	
Fair Value Through Profit & Loss (FVTPL)	-	697	
- Stage1 / 2 impairment allowance , of which	-	-	
- amount eligible for T2	-	-	
Loans and advances – Net, of which:	**2,218,897**	**2,218,897**	
- Loans and advances to domestic banks	-	-	
- Loans and advances to domestic customers	-	1,761,543	
- Loans and advances to non-resident for operations abroad	-	16,768	
- Loans and advances to SMEs	-	142,214	
- Financing from Islamic banking window	-	356,972	
- Expected credit loss allowance , of which:	-	(58,600)	
- Stage 3 impairment allowance and Reserve interest & profit	-	**(31,794)**	
- Stage1 / 2 impairment allowance , of which	-	**(26,806)**	
- amount eligible for T2	-	**19,129**	h
- amount ineligible for T2	-	7,677	
Fixed assets	**22,864**	**22,864**	
- Intangibles(CET1 adjustment)		(3,491)	e
- Other fixed asset		(19,373)	
Other assets	**29,154**	**29,154**	
Other assets, of which		29,193	
- Stage1 / 2 impairment allowance , of which		(39)	
- amount eligible for T2		-	
- amount ineligible for T2		(39)	
Total Assets	**2,702,477**	**2,702,477**	
Capital & Liabilities			
Paid-up Capital, of which:	**164,966**	**164,966**	
- Amount eligible for CET1	-	164,966	a
Reserves & Surplus; of which	**223,384**	**223,384**	
- Amount eligible for CET1 (Legal reserve)		34,028	c
- Amount eligible for CET1 (Subordinated debt reserve)		11,400	d

BASEL II PILLAR III AND BASEL III Report *(continued)*

31 December 2020

11. BASEL III CAPITAL DISCLOSURE *(Continued)*

11.1 The 3 step approach to reconciliation *(Continued)*

Step 2: Expansion of Balance sheet under Regulatory scope of consolidation *(Continued)*

- Amount eligible for CET1 (Retained earnings)		46,897	b
- Proposed cash dividend(removed from retained earnings)	-	(9,748)	b
- Proposed stock dividend(removed from retained earnings)	-	-	
- Amount ineligible for CET1 (Special Reserve)	-	998	
- Amount eligible for AT1	-	124,000	f
- Amount ineligible for T2 (Impairment reserve)	-	10,127	
- Amount eligible for T2 (Investments Fair value gains)	-	2,719	i
- FVOCI investments fair value loss (CET1 adjustment)	-	(5,008)	e
- Fair value reserve	-	(1,777)	
Total Capital	**388,350**	**388,350**	

For the year ended 31 December 2020	2019 financial Statement	Under Regulatory scope of consolidation	Reference
Deposits from banks	135,244	135,244	
Customer deposits, of which	1,924,654	1,924,654	
- Deposits for customers	-	1,639,189	
- Deposits of Islamic Banking window	-	285,465	
Borrowings, of which:	**159,775**	**159,775**	
- From banks	159,775	159,775	
Borrowings in form of bonds, Debentures & sukuks, of which	**12,000**	**12,000**	
- Amount eligible for T2		600	g
- Amount ineligible for T2		11,400	
Other liabilities & provisions	**82,454**	**82,454**	
Other liabilities & provisions, of which		**81,066**	
- Stage 3 provision	-	-	
- Stage1 / 2 impairment allowance , of which	**-**	**1,388**	
- amount eligible for T2	**-**	**-**	
- amount ineligible for T2	**-**	**1,388**	
Total Capital & Liabilities	**2,702,477**	**2,702,477**	

BASEL II PILLAR III AND BASEL III Report *(continued)*

31 December 2020

11. BASEL III CAPITAL DISCLOSURE *(Continued)*

11.1 The 3 step approach to reconciliation *(Continued)*

Step 3: Step Reconciliation of Regulatory Capital:

	Common Equity Tier 1 capital: instruments and reserves (RO' 000)		
	For the year ended 31 December 2019	**Component of regulatory capital reported by Bank**	**Source based on reference numbers/letters of the balance sheet under the regulatory scope of consolidation from step 2**
1	Directly issued qualifying common share (and equivalent for non-joint stock companies) capital plus related stock surplus	164,966	a
2	Retained earnings	37,149	b
3	Accumulated other comprehensive income (and other reserves)	45,428	c+d
4	**Common Equity Tier 1 capital before regulatory adjustments**	**247,543**	
5	Prudential valuation adjustments	(8,499)	e
6	Deferred tax assets that rely on future profitability excluding those arising from temporary differences (net of related tax liability)	-	
7	**Total regulatory adjustments to Common equity Tier 1**	**(8,499)**	
8	**Common Equity Tier 1 capital (CET1)**	**239,044**	
9	Additional Tier 1 capital (AT1)	124,000	f
	Tier 1 capital (T1 = CET1 + AT1)	363,044	
9	Directly issued qualifying Tier 2 instruments plus related stock surplus	600	g
10	Expected credit loss allowance / Provisions	19,129	h
11	Fair value reserve of FVOCI investments	2,719	i
	Tier 2 capital before regulatory adjustments	**22,448**	
	Tier 2 capital: regulatory adjustments	**-**	
	Tier 2 capital (T2)	**22,448**	
	Total capital (TC = T1 + T2)	**385,492**	

* The Board of Directors have proposed cash dividend of 5%, which has been adjusted in the capital of the Bank.

BASEL II PILLAR III AND BASEL III Report *(continued)*

31 December 2020

11. BASEL III CAPITAL DISCLOSURE *(Continued)*

11.2 Main Features of regulatory capital

Table below discloses the key features of all the regulatory capital issued by the Bank;

1	ahlibank SAOG	Common Equity Share Capital	Subordinated debt (Basel III)	Perpetual Subordinated Bonds (Additional Tier1)	Perpetual Subordinated Bonds (Additional Tier1)	Perpetual Subordinated Bonds (Additional Tier1)
2	Unique identifier (eg CUSIP, ISIN or Bloomberg identifier for private placement)	NA	NA	NA	NA	NA
3	Governing law(s) of the instrument Regulatory treatment	The laws of Oman in the form of Royal Decrees, Ministerial Decisions and CMA and CBO Regulations	The laws of Oman in the form of Royal Decrees, Ministerial Decisions and CMA and CBO Regulations	The laws of Oman in the form of Royal Decrees, Ministerial Decisions and CMA and CBO Regulations	The laws of Oman in the form of Royal Decrees, Ministerial Decisions and CMA and CBO Regulations	The laws of Oman in the form of Royal Decrees, Ministerial Decisions and CMA and CBO Regulations
4	Transitional Basel III rules	Common Equity Tier 1	Tier II	Additional Tier I	Additional Tier I	Additional Tier I
5	Post-transitional Basel III rules	Common Equity Tier 1	Eligible	Eligible	Eligible	Eligible
6	Eligible at solo/ group/group & solo	Solo	Solo	Solo	Solo	Solo
7	Instrument type (types to be specified by each jurisdiction)	Common Equity Share Capital	Private Placement of Subordinated debt	Rights Issue of Perpetual Subordinated bonds	Private placement	Private placement
8	Amount recognised in regulatory capital (Currency in mil, as of most recent reporting date)	RO 164.966 million	RO 11.400 million	RO 50 million	RO 54 million	RO 20 million
9	Par value of instrument	RO 164.966 million	RO 12.000 million	RO 50 million	RO 54 million	RO 20 million
10	Accounting classification	Shareholders' Equity	Liability amortised cost	Equity	Equity	Equity
11	Original date of issuance	Bank started operations in 1997	*Refer to the below table	11-October-2017	17-December-2018	13- June-2019
12	Perpetual or dated	Perpetual	Dated	Perpetual	Perpetual	Perpetual
13	Original maturity date	No maturity	**Refer to the below table	No maturity	No maturity	No maturity
14	Issuer call subject to prior supervisory approval	No	No	Yes	Yes	Yes

BASEL II PILLAR III AND BASEL III Report *(continued)*

31 December 2020

11. BASEL III CAPITAL DISCLOSURE *(Continued)*

11.2 Main Features of regulatory capital *(Continued)*

15	Optional call date, contingent call dates and redemption amount	NA	NA	The Bank may, at the end of five years and every interest payment date thereafter, redeem all but not some, of the bonds at nominal value, subject to prior approval from CBO.	The Bank may, at the end of five years and every interest payment date thereafter, redeem all but not some, of the bonds at nominal value, subject to prior approval from CBO.	The Bank may, at the end of five years and every interest payment date thereafter, redeem all but not some, of the bonds at nominal value, subject to prior approval from CBO.
16	Subsequent call dates, if applicable	NA	NA			
	Coupons / dividends					
17	Fixed or floating dividend/coupon	Floating	Fixed	Fixed	Fixed	Fixed
18	Coupon rate and any related index	NA	4%-5%	7.50%	7.50%	7.50%
19	Existence of a dividend stopper	NA	No	NA	NA	NA
20	Fully discretionary, partially discretionary or mandatory	Fully discretionary	Mandatory	Fully discretionary	Fully discretionary	Fully discretionary
21	Existence of step up or other incentive to redeem	No	No	NA	NA	NA
22	Noncumulative or cumulative	Noncumulative	Noncumulative	Noncumulative	Noncumulative	Noncumulative
23	Convertible or non-convertible	Non-convertible	convertible	Non-convertible	Non-convertible	Non-convertible
24	If convertible, conversion trigger (s)	NA	Statutory approach	NA	NA	NA
25	If convertible, fully or partially	NA	May convert fully or Partially	NA	NA	NA
26	If convertible, conversion rate	NA	Average price *	NA	NA	NA
27	If convertible, mandatory or optional conversion	NA	Optional	NA	NA	NA
28	If convertible, specify instrument type convertible into	NA	CET 1	NA	NA	NA

BASEL II PILLAR III AND BASEL III Report *(continued)*

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11. BASEL III CAPITAL DISCLOSURE *(Continued)*

11.2 Main Features of regulatory capital *(Continued)*

29	If convertible, specify issuer of instrument it converts into	NA	ahlibank	NA	NA	NA
30	Write-down feature	Yes	Yes	Yes	Yes	Yes
31	If write-down, write-down trigger(s)	Statutory approach	Statutory approach	Statutory approach	Statutory approach	Statutory approach
32	If write-down, full or partial	Write down fully	May be written down partially	Full or partial	Full or partial	Full or partial
33	If write-down, permanent or temporary	Permanent	Permanent	Permanent	Permanent	Permanent
34	If temporary write-down, description of write-up mechanism	NA	NA	NA	NA	NA
35	Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	NA	Common Equity Share Capital	Subordinate to deposit holders, general creditors, holders of Tier 2 subordinated debt/ bonds/sukuk of the bank	Subordinate to deposit holders, general creditors, holders of Tier 2 subordinated debt/ bonds/sukuk of the bank	Subordinate to deposit holders, general creditors, holders of Tier 2 subordinated debt/ bonds/sukuk of the bank
36	Non-compliant transitioned features	No	No	No	No	No
37	If yes, specify non-compliant features	NA	NA	NA	NA	NA

Number Of Subordinated debt (as per Basel III) (RO '000)	Par value of instrument	Amount recognised in regulatory capital (Currency in mil, as of most recent reporting date)	*Original date of issuance	**Original maturity date
Subordinated debt 4	1,000	1,000	30-Sep-14	30-Sep-21
Subordinated debt 5	5,000	5,000	01-Oct-14	02-Oct-21
Subordinated debt 9	3,000	3,000	29-Jun-15	29-Jun-21
Subordinated debt 10	3,000	2,400	10-Jun-15	13-Jun-22
Total	12,000	11,400		

BASEL II PILLAR III AND BASEL III Report *(continued)*

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12. BASEL III LIQUIDITY DISCLOSURE

The below liquidity disclosure is prepared in accordance with the requirements of the CBO Circular BM 1127 'Basel III – Framework on Liquidity Coverage Ratio (LCR) and LCR disclosure standard' issued on 24 December 2014. The disclosure is based on average of three monthly data points.

LIQUIDITY COVERAGE RATIO (LCR) **Common Disclosure Template**			
			(RO '000)
		Total Unweighted Value (average)	**Total Weighted Value (average)**
High Quality Liquid Assets			
1	Total High Quality Liquid Assets (HQLA)	289,560	289,560
Cash Outflows			
2	Retail deposits and deposits from small business customers, of which:	451,917	25,071
3	Stable deposits	18,642	559
4	Less stable deposits	433,275	24,512
5	Unsecured wholesale funding, of which:	489,537	224,155
6	Operational deposits (all counterparties) and deposits in networks of cooperative banks	1,097	274
7	Non-operational deposits (all counterparties)	423,217	158,658
8	Unsecured debt	65,223	65,223
9	Secured wholesale funding	48,355	1,688
10	Additional requirements, of which		
11	Outflows related to derivative exposures and other collateral requirements	104,248	104,248
12	Outflows related to loss of funding on debt products	-	-
13	Credit and liquidity facilities	16,182	1,618
14	Other contractual funding obligations		
15	Other contingent funding obligations	93,912	4,696
16	**TOTAL CASH OUTFLOWS**	1,204,151	361,476
Cash Inflows			
17	Secured lending (e.g. reverse repos)	-	-
18	Inflows from fully performing exposures	118,112	94,739
19	Other cash inflows	122,782	104,248
20	**TOTAL CASH INFLOWS**	240,894	198,987
21	**TOTAL HQLA**		289,560
22	**TOTAL NET CASH OUTFLOWS**		162,489
23	**LIQUIDITY COVERAGE RATIO (%)**		178.20%

BASEL II PILLAR III AND BASEL III Report *(continued)*

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12. BASEL III LIQUIDITY DISCLOSURE *(Continued)*

NET STABLE FUNDING RATIO (NSFR)

Common Disclosure Template

The below Net Stable Funding Ratio (NSFR) disclosure is prepared in accordance with the requirements of the CBO letter vide circular reference 1147 issued on October 26, 2016.

NSFR disclosure is presented below based on positions as on 31 December 2019.

Bank has maintained NSFR levels of 101%-110% during the year.

Sr No.	Particulars	No Maturity	<6 Months	6 Months to < 1 Year	>=1 Year	Weighted Value
ASF ITEM						
1	**Capital**	395,240	-	-	-	395,240
2	Regulatory Capital	395,240	-	-	-	395,240
3	Other Capital Instruments					
4	**Retail Deposits and Deposits from small Business Customers**	287,495	47,387	109,508	67,949	472,933
5	Stable Deposit	99,704	377	587	522	96,156
6	Less Stable Deposit	187,791	47,010	108,921	67,427	376,777
7	**Wholesale Funding**	217,405	294,307	438,116	414,290	889,204
8	Operational	1,336	-	-	-	668
9	Other Wholesale Funding	216,069	294,307	438,116	414,290	888,536
10	**Liabilities with matching interdependent Assets**					
11	**Other Liabilities**	-	-	-	130,900	130,900
12	NSFR Derivative Liability	-	-	-	-	-
13	All other liabilities and equities not included in above categories	300,387	-	-	-	-
14	**Total ASF**					1,888,277
RSF ITEM						
15	**Total NSFR high-quality liquid assets (HQLA)**					13,753
16	**Deposits held at other financial institutions for operational purposes**	17,769	-	-	-	8,884
17	**Performing Loans and Securities**					
18	Performing loans to financial institutions secured by Level 1 HQLA	-	-	-	-	-
19	Performing loans to financial institutions secured by non- Level 1 HQLA and unsecured performing loans to financial institutions	-	159,998	2,983	-	25,491
20	Performing loans to non-financial corporate clients, loans to retail and small business customers, and loans to sovereigns, central banks and PSEs, of which	69,315	395,542	40,234	1,509,494	1,535,615
21	With a risk weight of less than or equal to 35% under the Basel II Standardised approach for credit risk	-	-	-	-	-
22	Performing residential mortgages, of which:	-	-	-	-	-
23	With a risk weight of less than or equal to 35% under the Basel II Standardised Approach for credit risk	-	-	-	53,322	34,659
24	Securities that are not in default and do not qualify as HQLA, including exchange-traded equities	-	-	-	6,979	5,247
25	**Assets with matching interdependent liabilities**					
26	**Other Assets:**					
27	Physical traded commodities, including gold	-	-	-	-	-
28	Assets posted as initial margin for derivative contracts and contributions to default funds of CCPs	-	-	-	-	-
29	NSFR derivative assets	-	1,365	-	157	1,521
30	NSFR derivative liabilities before deduction of variation margin posted	-	-	-	-	-
31	All other assets not included in the above categories	-	-	-	91,753	91,753
32	**Off-balance sheet items**	-	178,742	38,206	21,106	11,903
33	**Total RSF**	-	-	-	-	1,728,826
34	**NET STABLE FUNDING RATIO**	-	-	-	-	109.22%

BASEL II PILLAR III AND BASEL III Report *(continued)*

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12. BASEL III LIQUIDITY DISCLOSURE *(Continued)*

LEVERAGE RATIO (LR)
Common Disclosure Template

The below Leverage Ratio disclosure is prepared in accordance with the requirements of the CBO letter BSD/2017/BKUP/Leverage/564 – Implementation of Basel III Leverage Ratio issued on 27 August 2017.

(All amounts in OMR'000)

	Table 1: Summary comparison of accounting assets vs leverage ratio exposure measure		
	Item	**Current Quarter**	**Previous Quarter**
1	Total consolidated assets as per published financial statements	2,702,477	2,592,306
2	Adjustments for derivative financial instruments	5,696	7,292
3	Adjustment for securities financing transactions (i.e., repos and similar secured lending)	87,138	76,037
4	Adjustment for off-balance sheet items (i.e., conversion to credit equivalent amounts of off-balance sheet exposures)	88,432	89,615
5	Other adjustments	-	-
6	**Leverage ratio exposure**	**2,883,743**	**2,765,251**

	Table 2: Leverage ratio common disclosure template		
	Item	**Current Quarter**	**Previous Quarter**
1	On-balance sheet items (excluding derivatives and SFTs, but including collateral)	2,702,477	2,592,306
3	**Total on-balance sheet exposures** (excluding derivatives and SFTs) (sum of lines 1 and 2)	**2,702,477**	**2,592,306**
	Derivative Exposures		
4	Replacement cost associated with all derivatives transactions (i.e., net of eligible cash variation margin)	2,662	3,040
5	Add-on amounts for PFE associated with all derivatives transactions	3,034	4,252
11	Total derivative exposures (sum of lines 4 to 10)	**5,696**	**7,292**
	Securities financing transaction exposures		
12	Gross SFT assets (with no recognition of netting), after adjusting for sale accounting transactions	81,646	71,444
14	CCR exposure for SFT assets	5,492	4,593
16	**Total securities financing transaction exposures (sum of lines 12 to 15)**	**87,138**	**76,038**
	Other Off-balance sheet exposures		
17	Off-balance sheet exposure at gross notional amount	190,873	200,783
18	(Adjustments for conversion to credit equivalent amounts)	(102,441)	(111,168)
19	**Off-balance sheet items (sum of lines 17 and 18**)	**88,432**	**89,615**
	Capital and total exposures		
20	**Tier 1 capital**	372,792	358,545
21	**Total exposures (sum of lines 3, 11, 16 and 19)**	2,883,743	2,765,251
	Leverage Ratio		
22	**Basel III leverage ratio (%)**	**12.9%**	**13.0%**

BASEL II PILLAR III AND BASEL III Report *(continued)*

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12. BASEL III LIQUIDITY DISCLOSURE *(Continued)*

The financial statements and other related disclosures are also available on the Bank's website, to view it on the website refer the link http://ahlibank.om/investor-relations/financial-reports/.

The Basel II, Pillar III report is prepared in accordance with the requirements of Basel II, Pillar III disclosures as set out in the CBO circulars BM1009 and BM1027.

Basel III capital and liquidity disclosures are prepared in accordance with CBO Circular BM 1114 'Regulatory Capital and Composition of Capital Disclosure Requirements under Basel III' issued on 17 November 2013, CBO circular dated March 20, 2018 and BM 1127 'Basel III – Framework on Liquidity Coverage Ratio (LCR) and LCR disclosure standard" issued on 24 December 2014, respectively. The NSFR disclosure has been prepared in accordance to CBO Circular reference BM 1147 dated 26 October 2016. The Bank's disclosure on leverage was prepared as per CBO circular on leverage ratio, issued on 27 August 2017 and CBO circular No. BM 1157 on Implementation of Basel III Leverage Ratio Standard dated 30 December 2018.

For ahlibank SAOG

Hamdan Ali Nasser Al Hinai
Chairman

Date: 27 January 2021