



HSBC Bank Oman S.A.O.G.

Interim Condensed Financial Report
30 June 2016



Interim Condensed Financial Report – 30 June 2016

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Presentation of information

This document comprises the Interim Condensed Financial Report – 30 June 2016 for HSBC Bank Oman S.A.O.G. ('HBON') ('the Bank'). It contains Unaudited Interim Condensed Financial Statements, together with the Board of Directors Report, the Auditor's review report and the Summary of Unaudited Results.

Board of Directors' Report for the six months ended 30 June 2016

Dear Shareholders,

On behalf of the Board of Directors, I am pleased to present your bank's financial results for the six months ended 30 June 2016.

We have built on the positive momentum seen in the first quarter by remaining focused on our strategic objectives of growing revenues, streamlining processes and procedures and implementing the highest Global Standards. I am pleased to report that we managed to deliver a good quarter in spite of the continuing period of low oil prices that weigh heavily on consumer sentiment and economic performance.

Performance Summary

I am also pleased to announce encouraging results for the first half of 2016. Our first half performance shows a 51.9% increase in net profit to RO7.9m compared to RO5.2m for the same period in 2015, mainly due to higher operating income and lower operating expenses partly offset by higher loan impairment charges.

Net operating income, before loan impairment charges, increased by 3.6% to RO37.4m compared to RO36.1m for the same period last year during which we had some significant one-off transactions including the sale of our branches in India.

Net interest income grew by 10.0% to RO26.5m for the period ended 30 June 2016, up from RO24.1m for the same period in 2015, due to higher interest income from corporate lending coupled with rising yields from the investment of surplus liquidity in government securities, partially offset by lower interest income received from retail customers due to the run-off of high yield retail loans which were written some years ago in a higher interest rate environment. Net fee income decreased by 4.4% to RO6.5m for the period ended 30 June 2016, due to lower wealth management and custody fees, the latter as a result of subdued activity on the MSM.

Net trading income increased by 20.6% to RO4.1m compared to RO3.4m for the same period in 2015 due to higher foreign exchange volumes at improved margins as well as the non-repeat of the RO0.2m foreign exchange loss incurred in 2015.

Other operating income decreased to RO0.3m compared to RO1.9m for the same period in 2015 due to the non-repeat of the gain on the disposal of HBON's India operations of RO0.8m and other legacy investments of RO0.7m.

A net charge of RO3.4m has been reported for loan impairment charges compared to a net charge of RO2.2m for the same period in 2015. The bank saw retail-specific provisions of RO2.4m and a corporate general provision of RO1.8m, itself attributed to the strong growth in corporate loans and advances. These were partly offset by a net recovery of RO1.2m from corporate customers.

Operating expenses decreased by 10.5% to RO24.8m compared to RO27.7m for the same period in 2015 due to our continuing focus on firm cost control. Our Cost efficiency ratio improved to 66.3% compared to 76.6% for the same period in 2015.

Loans and advances, net of provisions and reserved interest, increased by 6.4% to RO1,399.1m compared to RO1,314.7m as at 30 June 2015 largely from our corporate loan book.

Customer deposits fell by 5.7% to RO1,834.3m compared to RO1,945.2m as at 30 June 2015, due to a continuing reduction in Government and corporate deposits as the rest of the market bid more aggressively for deposits. The net loans to deposits ratio (ADR) improved to 76.3% compared to 67.6% as at 30 June 2015.

HBON's capital adequacy ratio stood at 18.4% as at 30 June 2016 compared to 17.5% as at 30 June 2015, representing a continuing strong capital base for future growth.

Delivering the best customer experience

In Retail Banking and Wealth Management our momentum of customer acquisition across all asset products has continued. In Q2 we launched a Sukuk investment product for the first time in Oman, and we inaugurated key initiatives focusing on growth of salary transfers. We also offered our customers an opportunity to win cash prizes through a lucky draw scheme where they use their credit cards both in Oman and abroad.

We continued to enhance our digital banking penetration as we released a new version of our mobile banking App, which promises an enhanced and enriched experience to our customers. We have seen further improvement in the Customer Recommendation Index in our key segment of Premier in Q2 vs Q1 2016.

Whilst we have focused our energy on growth, we have spent an equal amount of time and effort towards deepening our understanding of our current acquisition approach and the content of our existing portfolio. This is to ensure that we are well positioned to avoid any risks arising due to the current economic situation.

In Commercial Banking, we have witnessed further corporate assets growth since the beginning of the year. In April we held our fourth “Growth Series” event, which is designed to provide ambitious small businesses in Oman with the insight and advice they need to prosper locally and internationally. This event was titled ‘Treasury Technology Day’ and explored the role of technology in growing businesses, facing future challenges and looked at the benefits that online systems bring to treasury management.

We were pleased to be appointed as the sole International Financial Adviser to PDO for their inaugural debt raising in the international debt markets. The appointment reflects HSBC's local strengths in Oman as well as its ability to bring HSBC Group's Global expertise into complex financial situations to the benefit of the Sultanate's financial system.

Investing in our people and the community

Reinforcing our commitment to identifying and developing local talent, we continued our programme of appointing more Omani nationals into senior positions in the bank. We also continued to invest in staff training focusing on fraud control and Anti Money Laundering & Sanctions.

Supporting the Bank's female staff to achieve their career aspirations, we developed a tailor made Springboard program that aims to help them identify clear and practical steps towards achieving their career and personal goals. This programme complements the bank's ongoing efforts to achieve gender diversity at all levels.

In the Corporate Sustainability arena the second quarter witnessed a number of voluntary activities in the Bank some of which were developed in partnership with different organizations including Oman Association for the Disabled and The Environment Society of Oman. In April a number of staff volunteers joined a beach cleaning campaign organized by the Ministry of Environment and Climate Affairs in Daymaniyat Islands.

During the Holy Month of Ramadan the bank organized a number of philanthropic activities, where staff were given the chance to volunteer with their time and efforts to make a positive contribution to the community. The Ramadan activities included distributing food hampers to needy families and Eid gifts to orphans.

Conclusion

For the remainder of the year, we are confident that the Bank is well positioned to take full advantage of the opportunities that will arise. With our prudent risk appetite we will be able to confront the challenges that lie ahead.

On behalf of the Board of Directors, I would like to thank all of our customers, staff and management for their commitment and dedication. Special thanks also go to the Central Bank of Oman and the Capital Market Authority for their continued support and guidance.

I would like to take this opportunity to express our deepest wishes to His Majesty Sultan Qaboos Bin Said on the occasion of the Renaissance Day, confirming our continuous and full support as he continues to lead the Sultanate to further prosperity and development.

David Eldon
Chairman

Summary of unaudited results for the six months period ended 30 June 2016

| | 30 June 2016 | 30 June 2015 | |
|---|---|--------------------------------------|------------|
| | RO'000 | RO'000 | Change (%) |
| Loans and advances net of provisions and reserved interest | 1,399,130 | 1,314,666 | 6.4 |
| Customer deposits | 1,834,278 | 1,945,163 | (5.7) |
| Net assets | 304,288 | 303,904 | 0.1 |
| * Net assets per share | 0.152 | 0.152 | - |
| | Six months period ended 30 June 2016 | Six months period ended 30 June 2015 | |
| | RO'000 | RO'000 | Change (%) |
| Net interest income | 26,536 | 24,099 | 10.1 |
| Net profit for the period | 7,855 | 5,169 | 51.9 |
| ** Earnings per share (annualised) | 0.008 | 0.005 | 60 |
| *** Capital adequacy ratio (CAR) | 18.40% | 17.47% | |

* *Net assets (book value) per share is calculated by dividing the net assets (book value) at 30 June by the average number of ordinary shares in issue at 30 June.*

** *Earnings per share (annualised) has been calculated by dividing the annualised net profit after tax attributable to ordinary shareholders for the period ended 30 June by the average number of ordinary shares in issue for the period.*

*** *Capital adequacy ratio has been calculated in accordance with the Basel Capital Adequacy Accord. The ratio represents the ratio of risk weighted assets to capital.*



Report on review of interim condensed financial information to the directors of HSBC Bank Oman SAOG

Introduction

We have reviewed the accompanying interim condensed statement of financial position of HSBC Bank Oman SAOG as of 30 June 2016, and the related interim condensed statements of comprehensive income, changes in equity and cash flows for the six month period then ended and notes, comprising a summary of significant accounting policies and other explanatory notes. Management is responsible for the preparation and presentation of this condensed interim financial information in accordance with International Accounting Standard (“IAS”) 34, ‘Interim Financial Reporting’ and the minimum disclosure requirements issued by the Capital Market Authority (“CMA”). Our responsibility is to express a conclusion on this condensed interim financial information based on our review.

Scope of review

We conducted our review in accordance with the International Standard on Review Engagements 2410, ‘Review of interim financial information performed by the independent auditor of the entity’. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying condensed interim financial information is not prepared, in all material respects, in accordance with International Accounting Standard (“IAS”) 34, ‘Interim Financial Reporting’ and the minimum disclosure requirements issued by the Capital Market Authority (“CMA”).

A handwritten signature in blue ink, appearing to read 'Prakash Chandra', is written over a light blue horizontal line.

27 July 2016

Muscat, Sultanate of Oman

**Unaudited interim condensed statement of comprehensive income for the six months period ended
30 June 2016**

| | | Quarter ended 30 June 2016 RO'000 | Quarter ended 30 June 2015 RO'000 | Six months period ended 30 June 2016 RO'000 | Six months period ended 30 June 2015 RO'000 |
|--|----|---|---|--|--|
| Interest income | 5 | 15,466 | 13,753 | 29,966 | 27,770 |
| Interest expense | 6 | (1,918) | (1,735) | (3,430) | (3,671) |
| Net interest income | | 13,548 | 12,018 | 26,536 | 24,099 |
| Fee income | | 4,086 | 3,845 | 7,754 | 7,511 |
| Fee expense | | (610) | (351) | (1,246) | (717) |
| Net fee income | | 3,476 | 3,494 | 6,508 | 6,794 |
| Net trading income | | 1,786 | 1,787 | 4,114 | 3,361 |
| Dividend income | | 2 | 137 | 116 | 293 |
| Other operating income – net | 7 | 137 | 45 | 159 | 1,575 |
| Net operating income before loan impairment charges and other credit risk provisions | | 18,949 | 17,481 | 37,433 | 36,122 |
| Loan impairment charges and other credit risk provisions - net of recoveries | 8 | (1,162) | (1,437) | (3,433) | (2,246) |
| Net operating income | | 17,787 | 16,044 | 34,000 | 33,876 |
| Operating expenses | 9 | (12,083) | (13,790) | (23,687) | (26,529) |
| Amortization of intangible assets | 10 | (572) | (572) | (1,143) | (1,143) |
| Total operating expenses | | (12,655) | (14,362) | (24,830) | (27,672) |
| Profit before tax | | 5,132 | 1,682 | 9,170 | 6,204 |
| Tax expense | | (780) | (293) | (1,315) | (1,035) |
| Profit for the period | | 4,352 | 1,389 | 7,855 | 5,169 |
| Other comprehensive income /(loss) | | | | | |
| Items that will be reclassified subsequently to profit or loss when specific conditions are met | | | | | |
| Available-for-sale investment | | | | | |
| - Fair value (loss) / gain | | 312 | 161 | (4,715) | 197 |
| - Fair value gain reclassified to profit or loss on disposal | | (195) | - | (195) | (646) |
| - Amount reclassified to profit or loss in respect of impairment | | - | 22 | - | 22 |
| - Income tax | | (102) | (13) | 585 | 36 |
| | | 15 | 170 | (4,325) | (391) |
| Exchange differences | | | | | |
| - Foreign exchange loss reclassified to profit or loss on disposal of India operations | | - | - | - | 216 |
| - Effect of currency translation | | - | (7) | - | 57 |
| | | - | (7) | - | 273 |
| Other comprehensive income / (loss) for the period - net of tax | | 15 | 163 | (4,325) | (118) |
| Total comprehensive income for the period | | 4,367 | 1,552 | 3,530 | 5,051 |
| Earnings per share – basic and diluted (RO) | | | | | |
| - for the period | 11 | 0.002 | 0.001 | 0.004 | 0.003 |
| - annualised | | 0.009 | 0.003 | 0.008 | 0.005 |

The accompanying notes on pages 11 to 27 form an integral part of these interim condensed financial statements.

Unaudited interim condensed statement of financial position as at 30 June 2016

| | | At 30 June 2016 | At 30 June 2015 | Audited At 31 December 2015 |
|---|-------|--------------------|--------------------|-----------------------------------|
| | Notes | RO'000 | RO'000 | RO'000 |
| Assets | | | | |
| Cash and balances with central banks | | 172,974 | 336,588 | 277,736 |
| Due from banks | | 49,011 | 152,972 | 10,271 |
| Loans and advances to customers - net | 12 | 1,399,130 | 1,314,666 | 1,200,808 |
| Financial investments | 13 | 535,733 | 469,032 | 632,920 |
| Other assets | 14 | 46,324 | 38,016 | 41,989 |
| Intangible assets | 15 | 6,666 | 8,951 | 7,809 |
| Property and equipment | 16 | 26,796 | 27,597 | 26,917 |
| Deferred tax assets | | 2,098 | 3,016 | 1,492 |
| Total assets | | 2,238,732 | 2,350,838 | 2,199,942 |
| Liabilities and equity | | | | |
| Liabilities | | | | |
| Due to banks | | 46,254 | 49,717 | 36,211 |
| Deposits from customers | 17 | 1,834,278 | 1,945,163 | 1,802,338 |
| Other liabilities | 18 | 50,792 | 48,796 | 50,172 |
| Current tax liabilities | | 2,897 | 2,472 | 2,343 |
| Deferred tax liabilities | | 223 | 786 | 362 |
| Total liabilities | | 1,934,444 | 2,046,934 | 1,891,426 |
| Equity | | | | |
| Share capital | 23 | 200,031 | 200,031 | 200,031 |
| Legal reserve | 24(a) | 36,277 | 34,984 | 36,277 |
| Foreign exchange reserve | 24(b) | - | (247) | - |
| Available-for-sale fair value reserve | 24(c) | (3,242) | 4,206 | 1,083 |
| Retained earnings | | 71,222 | 64,930 | 71,125 |
| Net / total equity | | 304,288 | 303,904 | 308,516 |
| Total liabilities and equity | | 2,238,732 | 2,350,838 | 2,199,942 |
| Net assets per share - RO | | 0.152 | 0.152 | 0.154 |
| <i>Off-balance sheet items:</i> | | | | |
| Contingent liabilities and commitments | | | | |
| - Documentary credits | | 42,093 | 70,916 | 69,079 |
| - Guarantees and performance bonds | | 367,014 | 377,114 | 368,064 |
| - Others | 19 | 814,281 | 1,097,259 | 1,125,236 |
| | | 1,223,388 | 1,545,289 | 1,562,379 |

The accompanying notes on pages 11 to 27 form an integral part of these interim condensed financial statements

The interim condensed financial statements were authorised for issue on 27 July 2016 in accordance with the resolution of the Board of Directors.

David Eldon
Chairman

Andrew Long
Chief Executive Officer

Unaudited interim condensed statement of changes in equity for the six months period ended 30 June 2016

| | Share capital RO'000 | Legal reserve RO'000 | Statutory reserve RO'000 | Foreign exchange reserve RO'000 | Available- for-sale fair value reserve RO'000 | Retained earnings RO'000 | Total RO'000 |
|--|----------------------------|----------------------------|--------------------------------|--|---|--------------------------------|-----------------|
| At 1 January 2015 | 200,031 | 34,984 | 1,446 | (497) | 4,597 | 69,316 | 309,877 |
| Total comprehensive income for the period | | | | | | | |
| Profit for the period | - | - | - | - | - | 5,169 | 5,169 |
| Other comprehensive income / (loss) for the period | | | | | | | |
| Exchange differences | - | - | 23 | 250 | - | - | 273 |
| Net movement in fair value of available-for-sale investments (net of tax) | - | - | - | - | (391) | - | (391) |
| Total other comprehensive income / (loss) for the period | - | - | 23 | 250 | (391) | - | (118) |
| Total comprehensive income / (loss) for the period | - | - | 23 | 250 | (391) | 5,169 | 5,051 |
| Transfer to retained profits on sale of India operations | - | - | (1,469) | - | - | 1,469 | - |
| Transaction with shareholders, recorded directly in equity | | | | | | | |
| Dividend paid for 2014 | - | - | - | - | - | (11,024) | (11,024) |
| At 30 June 2015 | 200,031 | 34,984 | - | (247) | 4,206 | 64,930 | 303,904 |
| At 1 January 2016 | 200,031 | 36,277 | - | - | 1,083 | 71,125 | 308,516 |
| Total comprehensive income / (loss) for the period | | | | | | | |
| Profit for the period | - | - | - | - | - | 7,855 | 7,855 |
| Other comprehensive (loss) for the period | | | | | | | |
| Net movement in fair value of available-for-sale investments (net of tax) | - | - | - | - | (4,325) | - | (4,325) |
| Total other comprehensive (loss) for the period | - | - | - | - | (4,325) | - | (4,325) |
| Total comprehensive income / (loss) for the period | - | - | - | - | (4,325) | 7,855 | 3,530 |
| Transaction with shareholders, recorded directly in equity | | | | | | | |
| Dividend paid for 2015 | - | - | - | - | - | (7,758) | (7,758) |
| At 30 June 2016 | 200,031 | 36,277 | - | - | (3,242) | 71,222 | 304,288 |

The accompanying notes on pages 11 to 27 form an integral part of these interim condensed financial statements

Unaudited interim condensed statement of cash flows for the six months period ended 30 June 2016

| | <i>Notes</i> | Six months ended 30 June 2016 RO'000 | Six months ended 30 June 2015 RO'000 |
|--|--------------|---|---|
| Cash flows from operating activities | | | |
| Profit before tax | | 9,170 | 6,204 |
| Adjustments for: | | | |
| – Loan impairment charges and other credit risk provisions – net of recoveries | 8 | 3,433 | 2,246 |
| – Depreciation of property and equipment | 9 | 847 | 969 |
| – Amortisation of intangible assets | 10 | 1,143 | 1,143 |
| – Net gain on sale of financial investments | 7 | (90) | (664) |
| – Gain on sale of property and equipment | 7 | - | (25) |
| – Amortisation of financial investment | | (352) | 114 |
| – Gain on sale of India operations | 7 | - | (815) |
| – Employer's current service cost, with interest | | 83 | 110 |
| – Finance leases charge | | 41 | 51 |
| – Effect of currency translation | | - | (44) |
| – Change in operating assets | 28(a) | (206,091) | (157,546) |
| – Change in operating liabilities | 28(b) | 32,898 | 102,328 |
| – Retirement benefits paid | | (169) | (56) |
| – Tax paid | | (920) | (915) |
| Net cash used in operating activities | | (160,007) | (46,900) |
| Cash flows from investing activities | | | |
| Purchase of financial investments | | (755,064) | (3,130,845) |
| Proceeds from maturity of financial investments | | 847,784 | 3,326,313 |
| Purchase of property and equipment | | (726) | (1,487) |
| Proceeds from sale of property and equipment | | - | 680 |
| Cash out flow from sale of India operation, net of cash and cash equivalents | | - | (2,544) |
| Net cash generated from investing activities | | 91,994 | 192,117 |
| Cash flows from financing activities | | | |
| Dividends paid | | (7,758) | (11,024) |
| Finance leases paid | | (294) | (293) |
| Net cash used in financing activities | | (8,052) | (11,317) |
| Net change in cash and cash equivalents | | (76,065) | 133,900 |
| Cash and cash equivalents at the beginning of the year | | 251,796 | 290,057 |
| Cash and cash equivalents at the end of the year | 28 | 175,731 | 423,957 |

The accompanying notes on pages 11 to 27 form an integral part of these interim condensed financial statements.

1 Legal status and activities

HSBC Bank Oman S.A.O.G. ('the Bank' or 'HBON') is an Omani joint stock company, which was incorporated on 1 January 1979, operating as a commercial bank through a network of branches in the Sultanate of Oman. The registered address of the Bank is P.O. Box 1727, CPO Seeb, Postal Code 111, Sultanate of Oman. The Bank has its shares listed on Muscat Securities Market.

HSBC Middle East Holdings BV ('HMEH') holds 51% of the shares in HBON. The ultimate parent company of HBON is HSBC Holdings plc.

2 Basis of preparation

(a) Compliance with International Financial Reporting Standards

The interim condensed financial statements of the Bank have been prepared in accordance with IAS 34 'Interim Financial Reporting' ('IAS 34') as issued by the International Accounting Standards Board ('IASB'), the disclosure requirements set out in the Rules for Disclosure and Proformas issued by the Capital Market Authority ('CMA'), and the Commercial Companies Law of 1974, as amended, of the Sultanate of Oman and the applicable regulations of the Central Bank of Oman ("CBO").

The audited financial statements of the Bank as at and for the year ended 31 December 2015 were prepared in accordance with International Financial Reporting Standards ('IFRSs') as issued by the IASB, the disclosure requirements of CMA and the applicable regulations of the CBO.

IFRSs comprise accounting standards issued by the IASB and its predecessor body as well as interpretations issued by the International Financial Reporting Interpretations Committee ('IFRIC') and its predecessor body.

(b) Presentation of information

The functional currency of the Bank is Rials Omani ("RO"), which is also the presentation currency of the interim condensed financial statements of the Bank.

(c) Corresponding figures

These interim condensed financial statements include corresponding figures information as required by IAS 34 and CMA.

(d) Use of estimates and assumptions

The preparation of financial information requires the use of estimates and assumptions about future conditions. The use of available information and the application of judgement are inherent in the formation of estimates; actual results in the future may differ from those reported. Management believes that the Bank's critical accounting policies where judgement is necessarily applied are those which relate to the valuation of separately identifiable assets and liabilities acquired during merger, the useful lives of intangible assets, impairment of loans and advances, the valuation of financial instruments and the impairment of available-for-sale financial assets.

Notes to the unaudited interim condensed financial statements (continued)

2 Basis of preparation (continued)

(e) Future accounting developments

A number of new standards and amendments to standards and interpretations are effective for annual periods beginning on or after 1 January 2017. None of these are expected to have a significant effect on the interim condensed financial statements of the Bank except the following set out below:

IFRS 9, 'Financial instruments', addresses the classification, measurement and recognition of financial assets and financial liabilities. The complete version of IFRS 9 was issued in July 2014. It replaces the guidance in IAS 39 that relates to the classification and measurement of financial instruments. IFRS 9 retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortised cost, fair value through other comprehensive income and fair value through profit or loss. There is now a new expected credit losses model that replaces the incurred loss impairment model used in IAS 39.

The mandatory application date for IFRS 9 as a whole is 1 January 2018, but it is possible to apply the revised presentation for certain liabilities measured at fair value from an earlier date. The Bank is currently assessing the impact of IFRS 9 will have on the financial statements but due to the complexity of the classification and measurement, impairment, and hedge accounting requirements and their inter-relationship, it is not possible at this stage to quantify the potential impact as at the date of the approval of these interim condensed financial statements.

IFRS 15, 'Revenue from Contracts with Customers', will replace IAS 18 which covers contracts for goods and services and IAS 11 which covers construction contracts. This new standard is based on the principle that revenue is recognised when control of a good or service transfers to a customer – so the notion of control replaces the existing notion of risks and rewards. The standard permits a modified retrospective approach for the adoption. Under this approach entities will recognise transitional adjustments in retained earnings on the date of initial application, i.e. without restating the comparative period. They will only need to apply the new rules to contracts that are not completed as of the date of initial application. The mandatory application date for IFRS 15 is 1 January 2018. The Bank is currently assessing the impact of this standard but it is not practicable to quantify the potential effect at the date of approval of these interim condensed financial statements.

IFRS 16, 'Leases', replaces the current guidance in IAS 17 and is a far-reaching change in accounting by lessees in particular. Under IAS 17, lessees were required to make a distinction between a finance lease (on balance sheet) and an operating lease (off balance sheet). IFRS 16 now requires lessees to recognise a lease liability reflecting future lease payments and a 'right-of-use asset' for virtually all lease contracts. It includes an optional exemption for certain short-term leases and leases of low-value assets; however, this exemption can only be applied by lessees.

For lessors, the accounting stays almost the same. However, as the it has updated the guidance on the definition of a lease (as well as the guidance on the combination and separation of contracts), lessors will also be affected by the new standard. At the very least, the new accounting model for lessees is expected to impact negotiations between lessors and lessees.

Under IFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. The mandatory application date for IFRS 16 is 1 January 2019 with earlier application permitted if IFRS 15, 'Revenue from Contracts with Customers', is also applied. The Bank is currently assessing the impact of this standard but it is not practicable to quantify the potential effect at the date of approval of these interim condensed financial statements.

3 Accounting policies

The accounting policies applied by the Bank in these interim condensed financial statements are the same as those applied by the Bank in its financial statements as at and for the year ended 31 December 2015.

There are no standards, interpretations or amendments to existing standards that are effective for the first time for the financial year beginning on 1 January 2016 which have a material impact on the interim condensed financial statements.

Notes to the unaudited interim condensed financial statements (continued)

4 Products and services

The Bank provides a comprehensive range of banking and related financial services to its customers.

- Retail Banking and Wealth Management ('RBWM') offers a broad range of products and services to meet the personal banking needs, consumer finance and wealth management needs of individual customers. Typically, customer offerings include personal banking products (current and savings accounts, mortgages and personal loans, credit cards, debit cards and local and international payment services) and wealth management services (insurance and investment products and financial planning services).
- Commercial Banking ('CMB') product offerings include the provision of receivables financing services, payments and cash management, international trade finance, treasury and capital markets, commercial cards, cash and derivatives in foreign exchange and rates, and online and direct banking offerings.
- Global Banking and Markets ('GB&M') provides tailored financial solutions to government, corporate and institutional clients. The client focused business lines deliver a full range of banking capabilities including financing, advisory and transaction services; a markets business that provides services in credit, rates, foreign exchange, money markets and securities services; and principal investment activities.

5 Interest income

Interest bearing assets earned interest at an overall annualized rate of 3.13% for the six months period ended 30 June 2016 (30 June 2015 – 2.83%).

| | Six months period ended 30 June 2016 RO'000 | Six months period ended 30 June 2015 RO'000 |
|---------------------------------|--|---|
| Loans and advances to customers | 27,130 | 25,898 |
| Financial investments | 2,232 | 1,048 |
| Due from banks | 180 | 269 |
| Others | 424 | 555 |
| | 29,966 | 27,770 |

6 Interest expense

For the six months period ended 30 June 2016, the average overall annualised cost of funds was 0.37% (30 June 2015 – 0.38%).

| | Six months period ended 30 June 2016 RO'000 | Six months period ended 30 June 2015 RO'000 |
|-------------------------|--|---|
| Deposits from customers | (3,430) | (3,484) |
| Due to banks | - | (187) |
| | (3,430) | (3,671) |

Notes to the unaudited interim condensed financial statements (continued)

7 Other operating income - net

| | Six months period ended 30 June 2016 RO'000 | Six months period ended 30 June 2015 RO'000 |
|--|---|---|
| Gain on sale of India operations | - | 815 |
| Gain on sale of financial investments | 90 | 664 |
| Gain on sale of property and equipment | - | 25 |
| Impairment of available-for-sale equity securities | - | (22) |
| Other income | 69 | 93 |
| | <u>159</u> | <u>1,575</u> |

8 Loan impairment charges and other credit risk provisions - net of recoveries

| | Six months period ended 30 June 2016 RO'000 | Six months period ended 30 June 2015 RO'000 |
|---|---|---|
| Provided during the period – general (note 12) | (2,224) | (1,713) |
| Provided during the period – specific (note 12) | (3,726) | (3,550) |
| Provisions released / written back (note 12) | 1,494 | 1,574 |
| Adjustments as a result of fair value unwind | 229 | 301 |
| Reserved interest released | 27 | 214 |
| Written-off loans recovered | 1,034 | 1,201 |
| Bad debts directly written off to statement of comprehensive income | (267) | (273) |
| | <u>(3,433)</u> | <u>(2,246)</u> |

9 Operating expenses

| | Six months period ended 30 June 2016 RO'000 | Six months period ended 30 June 2015 RO'000 |
|--|---|---|
| Employee compensation and benefits | (11,865) | (12,380) |
| General and administrative expenses* | (10,975) | (13,180) |
| Depreciation of property and equipment | (847) | (969) |
| | <u>(23,687)</u> | <u>(26,529)</u> |

* General and administrative expenses for the current period include the RO0.8m of “Mandoos Prize” draw expenses (30 June 2015: RO0.6m).

10 Amortisation of intangible assets

| | Six months period ended 30 June 2016 RO'000 | Six months period ended 30 June 2015 RO'000 |
|--|---|---|
| This represents amortisation of intangible assets as result of business combination accounted for as follows : | | |
| Core deposits | (880) | (880) |
| Customer relationships | (263) | (263) |
| | <u>(1,143)</u> | <u>(1,143)</u> |

Notes to the unaudited interim condensed financial statements (continued)

11 Earnings per share – basic and diluted

Earnings per share is calculated by dividing the profit attributable to the shareholders by the weighted average number of shares in issue, as follows:

| | Six months period ended 30 June 2016 | Six months period ended 30 June 2015 | For the year ended 31 December 2015 |
|--|---|---|--|
| Weighted average number of shares in issue ('000) | 2,000,312 | 2,000,312 | 2,000,312 |
| Net profit for the period / year (RO'000) | 7,855 | 5,169 | 12,930 |
| Earnings per share – basic and diluted (RO) | | | |
| - for the period | 0.004 | 0.003 | 0.006 |
| - annualised | 0.008 | 0.005 | 0.006 |

12 Loans and advances to customers - net

To comply with the CBO regulations, the table below includes the provision for loan impairment on loans acquired in the business combination.

| | 30 June 2016 RO'000 | 30 June 2015 RO'000 | 31 December 2015 RO'000 |
|--|------------------------------------|---------------------------|-------------------------------|
| Overdrafts | 81,599 | 71,406 | 66,130 |
| Loans | 1,380,552 | 1,301,052 | 1,204,540 |
| Bills discounted / purchased | 16,988 | 30,491 | 13,394 |
| Gross loans and advances | 1,479,139 | 1,402,949 | 1,284,064 |
| Provision for loan impairment - specific | (27,108) | (28,676) | (28,380) |
| Provision for loan impairment - general* | (18,659) | (17,590) | (16,435) |
| Reserved interest | (34,242) | (42,017) | (38,441) |
| Net loans and advances | 1,399,130 | 1,314,666 | 1,200,808 |

* General provision comprises provision on a portfolio basis for loans and advances to customers.

The interest rate bands of gross loans and advances to customers are as follows:

| | 30 June 2016 RO'000 | 30 June 2015 RO'000 | 31 December 2015 RO'000 |
|---------------|------------------------------------|---------------------------|-------------------------------|
| 0-5% | 990,212 | 858,516 | 762,308 |
| 5-7% | 343,940 | 348,634 | 350,213 |
| 7-10% | 95,545 | 133,178 | 112,787 |
| 10-13% | 25,395 | 44,407 | 37,687 |
| more than 13% | 24,047 | 18,214 | 21,069 |
| | 1,479,139 | 1,402,949 | 1,284,064 |

Maturity analysis of net loans and advances to customers as per CBO circular BM 955 is as follows:

| | 30 June 2016 RO'000 | 30 June 2015 RO'000 | 31 December 2015 RO'000 |
|-------------------|------------------------------------|---------------------------|-------------------------------|
| 0-6 months | 554,071 | 509,771 | 413,261 |
| 6-12 months | 19,155 | 17,417 | 3,865 |
| 1-3 years | 36,767 | 54,650 | 57,421 |
| 3-5 years | 134,789 | 138,704 | 132,156 |
| More than 5 years | 654,348 | 594,124 | 594,105 |
| | 1,399,130 | 1,314,666 | 1,200,808 |

12 Loans and advances to customers – net (continued)

Concentration of loans and advances:

Loans and advances to customers by industry sector

| | 30 June 2016 RO'000 | 30 June 2015 RO'000 | 31 December 2015 RO'000 |
|---|------------------------------------|---------------------------|-------------------------------|
| Personal and consumer loans | 486,528 | 468,531 | 466,752 |
| Corporate and commercial | | | |
| Import trade | 251,603 | 208,977 | 165,280 |
| Construction | 54,018 | 79,820 | 86,934 |
| Manufacturing | 307,902 | 218,000 | 218,935 |
| Wholesale and retail trade | 57,906 | 49,068 | 45,217 |
| Export trade | - | 5,194 | - |
| Electricity, gas, water, transportation and communication | 104,952 | 116,438 | 90,854 |
| Services | 140,691 | 223,596 | 148,316 |
| Mining and quarrying | 11,192 | 23,303 | 12,528 |
| Others | 64,347 | 10,022 | 49,248 |
| | 992,611 | 934,418 | 817,312 |
| Financial institutions | - | - | - |
| Total gross loans and advances | 1,479,139 | 1,402,949 | 1,284,064 |
| Provision for loan impairment - specific | (27,108) | (28,676) | (28,380) |
| Provision for loan impairment - general | (18,659) | (17,590) | (16,435) |
| Reserved interest | (34,242) | (42,017) | (38,441) |
| Net loans and advances | 1,399,130 | 1,314,666 | 1,200,808 |
| Non performing loans | 66,474 | 78,276 | 71,881 |

Specific provision for loan impairment and reserved interest represents 92.3% (30 June 2015 – 90.3% and 31 December 2015 – 93%) of gross non-performing loans and advances.

Notes to the unaudited interim condensed financial statements (continued)

12 Loans and advances to customers (continued)

Provision for loan impairment and reserved interest

The movement on provision for loan impairment for the six months period ended 30 June 2016 is analysed in the table below:

| | Specific provision RO'000 | General provision RO'000 | Total provision RO'000 |
|---|---------------------------------|--------------------------------|------------------------------|
| Balance at 1 January 2016 | 28,380 | 16,435 | 44,815 |
| Provided during the period (note 8) | 3,726 | 2,224 | 5,950 |
| Provisions released / written back (note 8) | (1,494) | - | (1,494) |
| Written off during the period | (3,504) | - | (3,504) |
| Balance at 30 June 2016 | 27,108 | 18,659 | 45,767 |

The movement on provision for loan impairment for the six months period ended 30 June 2015 is analysed in the table below:

| | Specific provision RO'000 | General provision RO'000 | Total Provision RO'000 |
|--|---------------------------------|--------------------------------|------------------------------|
| Balance at 1 January 2015 | 36,192 | 15,880 | 52,072 |
| Currency translation effect on opening balance | (7) | - | (7) |
| Movement due to sale of India operations | - | (3) | (3) |
| Provided during the period (note 8) | 3,550 | 1,713 | 5,263 |
| Provisions released / written back (note 8) | (1,574) | - | (1,574) |
| Written off during the period | (9,485) | - | (9,485) |
| Balance at 30 June 2015 | 28,676 | 17,590 | 46,266 |

The movement on reserved interest for the period is analysed below:

| | 30 June 2016 RO'000 | 30 June 2015 RO'000 |
|---|------------------------------------|---------------------------|
| Balance at the beginning of the period | 38,441 | 47,774 |
| Currency translation effect on opening balance | - | (1) |
| Reserved during the period | 4,022 | 4,822 |
| Released to the statement of comprehensive income | (406) | (597) |
| Written off during the period | (7,815) | (9,981) |
| Balance at end of the period | 34,242 | 42,017 |

The estimated fair value of loans and advances is RO1,367.1m as of 30 June 2016 (30 June 2015 - RO1,292.2m and 31 December 2015 – RO1,180.0).

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Notes to the unaudited interim condensed financial statements (continued)

13 Financial investments – classified as available for sale

Financial investments details are provided as follows:

| | Fair value 30 June 2016 RO'000 | Fair value 30 June 2015 RO'000 | Fair value 31 December 2015 RO'000 | Carrying value 30 June 2016 RO'000 | Carrying value 30 June 2015 RO'000 | Carrying value 31 December 2015 RO'000 | Cost 30 June 2016 RO'000 | Cost 30 June 2015 RO'000 | Cost 31 December 2015 RO'000 |
|--|---|---|---|---|--|--|---|-----------------------------------|---------------------------------------|
| Marketable securities – MSM | | | | | | | | | |
| Finance | - | 2,467 | 2,288 | - | 2,467 | 2,288 | - | 1,911 | 1,911 |
| Insurance | 378 | 398 | 398 | 378 | 398 | 398 | 334 | 340 | 340 |
| Industrial | - | 33 | - | - | 33 | - | - | 33 | - |
| Government bonds | 82,353 | 44,214 | 85,424 | 82,353 | 44,214 | 85,424 | 86,750 | 43,569 | 85,036 |
| | 82,731 | 47,112 | 88,110 | 82,731 | 47,112 | 88,110 | 87,084 | 45,853 | 87,287 |
| Marketable securities – Foreign by Sector | | | | | | | | | |
| Foreign shares | - | 5,446 | - | - | 5,446 | - | - | 2,340 | - |
| | - | 5,446 | - | - | 5,446 | - | - | 2,340 | - |
| Unquoted and other investments | | | | | | | | | |
| Certificates of deposits | - | 198,309 | - | - | 198,309 | - | - | 198,311 | - |
| Treasury bills | 448,875 | 212,972 | 540,957 | 448,875 | 212,972 | 540,957 | 448,422 | 213,088 | 540,496 |
| Unquoted Omani shares* | 260 | 1,010 | 260 | 260 | 1,010 | 260 | 260 | 1,010 | 260 |
| Unquoted foreign shares* | 67 | 67 | 67 | 67 | 67 | 67 | 67 | 67 | 67 |
| Investment fund units | 3,800 | 4,116 | 3,526 | 3,800 | 4,116 | 3,526 | 3,590 | 3,590 | 3,590 |
| | 453,002 | 416,474 | 544,810 | 453,002 | 416,474 | 544,810 | 452,339 | 416,066 | 544,413 |
| Total | 535,733 | 469,032 | 632,920 | 535,733 | 469,032 | 632,920 | 539,423 | 464,259 | 631,700 |

*Unquoted Omani shares and unquoted foreign shares are carried at cost.

Notes to the unaudited interim condensed financial statements (continued)

13 Financial investments (continued)

| Details of AFS investments are as follows: | 30 June 2016 RO'000 | 30 June 2015 RO'000 | 31 December 2015 RO'000 |
|--|------------------------------------|---------------------------|-------------------------------|
| Cost of: | | | |
| Quoted - Equity and other investments | 87,084 | 48,193 | 87,287 |
| Unquoted and other investments | 452,339 | 416,066 | 544,413 |
| | 539,423 | 464,259 | 631,700 |
| Revaluation gain / (loss) of: | | | |
| Quoted equity and other securities | (3,690) | 4,773 | 1,220 |
| | 535,733 | 469,032 | 632,920 |

14 Other assets

| | 30 June 2016 RO'000 | 30 June 2015 RO'000 | 31 December 2015 RO'000 |
|---------------------------------------|------------------------------------|---------------------------|-------------------------------|
| Acceptances | 30,870 | 29,179 | 35,477 |
| Derivatives - positive mark to market | 6,057 | 3,420 | 3,733 |
| Prepayments and accrued income | 1,189 | 1,994 | 1,159 |
| Others | 8,208 | 3,423 | 1,620 |
| | 46,324 | 38,016 | 41,989 |

15 Intangible assets

| | 30 June 2016 RO'000 | 30 June 2015 RO'000 | 31 December 2015 RO'000 |
|------------------------|------------------------------------|---------------------------|-------------------------------|
| Core deposits | 12,306 | 12,306 | 12,306 |
| Customer relationships | 3,691 | 3,691 | 3,691 |
| | 15,997 | 15,997 | 15,997 |
| Less: amortised | (9,331) | (7,046) | (8,188) |
| | 6,666 | 8,951 | 7,809 |

16 Property and equipment

RO0.7m of property and equipment were added during the period (30 June 2015: RO1.5m). Property and equipment disposed of during the period was nil (30 June 2015: RO1.1m).

17 Deposits from customers

| Deposits details are as follows: | 30 June 2016 RO'000 | 30 June 2015 RO'000 | 31 December 2015 RO'000 |
|----------------------------------|------------------------------------|---------------------------|-------------------------------|
| Current and call | 865,665 | 1,019,100 | 965,245 |
| Savings | 479,905 | 479,750 | 470,161 |
| Time deposits | 486,347 | 442,968 | 364,589 |
| Others | 2,361 | 3,345 | 2,343 |
| | 1,834,278 | 1,945,163 | 1,802,338 |

Notes to the unaudited interim condensed financial statements (continued)

17 Deposits from customers (continued)

Maturity analysis of customer deposits as per CBO circular BM 955 is as follows:

| | 30 June 2016 RO'000 | 30 June 2015 RO'000 | 31 December 2015 RO'000 |
|--------------|------------------------------------|---------------------------|-------------------------------|
| 0-6 months | 636,146 | 790,511 | 667,110 |
| 6-12 months | 317,144 | 262,907 | 264,531 |
| 1-3 years | 345,743 | 145,608 | 141,645 |
| 3-5 years | 152,590 | 328,381 | 327,574 |
| Over 5 years | 382,655 | 417,756 | 401,478 |
| | 1,834,278 | 1,945,163 | 1,802,338 |

The interest rate bands of deposits are as follows:

| | 30 June 2016 RO'000 | 30 June 2015 RO'000 | 31 December 2015 RO'000 |
|------|------------------------------------|---------------------------|-------------------------------|
| 0-2% | 1,558,294 | 1,758,581 | 1,614,614 |
| 2-4% | 275,984 | 186,571 | 187,724 |
| 6-8% | - | 11 | - |
| | 1,834,278 | 1,945,163 | 1,802,338 |

18 Other liabilities

| | 30 June 2016 RO'000 | 30 June 2015 RO'000 | 31 December 2015 RO'000 |
|---------------------------------------|------------------------------------|---------------------------|-------------------------------|
| Derivatives – negative mark to market | 1,442 | 531 | 204 |
| Retirement benefit liability | 550 | 500 | 636 |
| Acceptances | 30,870 | 29,179 | 35,477 |
| Provisions | 216 | 1,177 | 535 |
| Accruals and deferred income | 3,010 | 5,472 | 4,930 |
| Obligation under finance lease | 711 | 911 | 964 |
| Others | 13,993 | 11,026 | 7,426 |
| | 50,792 | 48,796 | 50,172 |

19 Contingent liabilities, commitments and derivatives

| | 30 June 2016 RO'000 | 30 June 2015 RO'000 | 31 December 2015 RO'000 |
|---|------------------------------------|---------------------------|-------------------------------|
| Forward forex contracts outstanding | 178,430 | 283,162 | 266,857 |
| Interest rate swaps - notional | 77,000 | 91,836 | 77,000 |
| Undrawn unconditionally cancellable commitments | 474,679 | 500,219 | 576,767 |
| Undrawn unconditionally non-cancellable commitments | 84,172 | 222,042 | 204,612 |
| | 814,281 | 1,097,259 | 1,125,236 |

Notes to the unaudited interim condensed financial statements (continued)

19 Contingent liabilities, commitments and derivatives (continued)

As at 30 June 2016, there were certain legal suits pending against the Bank. Based on the opinion of the Bank's legal counsel, the Bank's management believes that no additional liability is expected to arise from these cases and therefore the management does not consider it necessary to make any additional provisions in this regard.

20 Basis of valuation for financial assets and liabilities measured at fair value

| | <u>Valuation techniques</u> | | Total RO'000 |
|---|---|--|-----------------|
| | Quoted market price Level 1 RO'000 | Using observable inputs Level 2 RO'000 | |
| At 30 June 2016 | | | |
| Assets | | | |
| Derivatives | - | 6,057 | 6,057 |
| Financial investments: available-for-sale | 82,731 | 452,675 | 535,406 |
| Liabilities | | | |
| Derivatives | - | 1,442 | 1,442 |
| At 30 June 2015 | | | |
| Assets | | | |
| Derivatives | - | 3,420 | 3,420 |
| Financial investments: available-for-sale | 52,558 | 415,397 | 467,955 |
| Liabilities | | | |
| Derivatives | - | 531 | 531 |
| At 31 December 2015 | | | |
| Assets | | | |
| Derivatives | - | 3,733 | 3,733 |
| Financial investments: available-for-sale | 88,110 | 544,483 | 632,593 |
| Liabilities | | | |
| Derivatives | - | 204 | 204 |

Investments carried at cost and derivatives

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

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

Foreign exchange contracts are valued based on market prices. The market value adjustment of foreign exchange contracts are included in the book value of other assets.

There has been no change to the basis of valuation of level 2 financial assets and liabilities disclosed in the latest audited financial statements of the Bank for the year ended 31 December 2015.

Notes to the unaudited interim condensed financial statements (continued)

21 Asset liability mismatch

The asset liability mismatch is based on CBO circular BM 955 and given as follows:

| Maturities | 30 June 2016 | | | 30 June 2015 | | | 31 December 2015 | | |
|-------------------|------------------|------------------------|-----------|------------------|------------------------|-----------|------------------|------------------------|-----------|
| | Assets | Liabilities and equity | Mismatch | Assets | Liabilities and equity | Mismatch | Assets | Liabilities and equity | Mismatch |
| | RO'000 | RO'000 | RO'000 | RO'000 | RO'000 | RO'000 | RO'000 | RO'000 | RO'000 |
| 0-6 months | 1,221,265 | 736,147 | 485,118 | 1,308,692 | 892,152 | 416,540 | 1,092,553 | 755,864 | 336,689 |
| 6-12 months | 58,204 | 325,164 | (266,960) | 101,606 | 268,567 | (166,961) | 166,033 | 278,326 | (112,293) |
| 1-3 years | 78,580 | 345,743 | (267,163) | 95,600 | 145,608 | (50,008) | 97,689 | 141,645 | (43,956) |
| 3-5 years | 180,574 | 152,590 | 27,984 | 172,604 | 328,381 | (155,777) | 194,484 | 327,574 | (133,090) |
| more than 5 years | 700,109 | 679,088 | 21,021 | 672,336 | 716,130 | (43,794) | 649,183 | 696,533 | (47,350) |
| | 2,238,732 | 2,238,732 | - | 2,350,838 | 2,350,838 | - | 2,199,942 | 2,199,942 | - |

22 Exposure to credit risk

| | Loans and advances (As per CBO) | | | Due from banks | | | Financial investments | | |
|--|---------------------------------|------------------|------------------|----------------|----------------|------------------|-----------------------|----------------|------------------|
| | 30 June 2016 | 30 June 2015 | December 31 2015 | 30 June 2016 | 30 June 2015 | December 31 2015 | 30 June 2016 | 30 June 2015 | 31 December 2015 |
| | RO'000 | RO'000 | RO'000 | RO'000 | RO'000 | RO'000 | RO'000 | RO'000 | RO'000 |
| Individually impaired – non performing | 66,474 | 78,276 | 71,881 | - | - | - | - | - | - |
| Provision for loan impairment specific and reserved interest | (61,350) | (70,693) | (66,821) | - | - | - | - | - | - |
| Carrying amount of non-performing | 5,124 | 7,583 | 5,060 | - | - | - | - | - | - |
| Past due and not impaired | 28,621 | 18,556 | 18,971 | - | - | - | - | - | - |
| Neither past due nor impaired | 1,384,044 | 1,306,117 | 1,193,212 | 49,011 | 152,972 | 10,271 | 535,733 | 469,032 | 632,920 |
| General provision | (18,659) | (17,590) | (16,435) | - | - | - | - | - | - |
| Total carrying amount | 1,399,130 | 1,314,666 | 1,200,808 | 49,011 | 152,972 | 10,271 | 535,733 | 469,032 | 632,920 |

23 Share capital

The share capital of the Bank is divided into 2,000,312,790 fully paid shares of RO0.100 each (30 June 2015 and 31 December 2015 – 2,000,312,790 shares of RO0.100 each). The authorised share capital of the Bank is 7,500 million shares of RO0.100 each (30 June 2015 and 31 December 2015 – 7,500 million shares of RO 0.100 each).

Major Shareholder

All those shareholders of the Bank who own 10% or more of the Bank’s shares in their name, and the number of shares they hold are as follows:

| | 30 June 2016 Number of shares | 30 June 2015 Number of shares | 31 December 2015 Number of shares |
|-------------------------------|--|--|--|
| HSBC Middle East Holdings BV | 1,020,159,523 | - | 1,020,159,523 |
| HSBC Bank Middle East Limited | - | 1,020,159,523 | - |

24 Reserves

(a) Legal reserve

In accordance with the Commercial Companies Law of Oman 1974 as amended, annual appropriations of 10% of the profit for the year are made to the legal reserve until the accumulated balance of the reserve is equal to one-third of the value of the Bank’s paid-up share capital. This reserve is not available for distribution.

(b) Foreign exchange reserve

Foreign exchange reserve represents exchange differences arising from the retranslation of opening foreign currency net investments, and exchange differences arising from retranslation of the result for the reporting period from the average rate to the exchange rate prevailing at the period end, recognised in other comprehensive income. Exchange differences on a monetary item that is part of a net investment in a foreign operation are recognised in other comprehensive income. On disposal of a foreign operation, exchange differences relating thereto and previously recognised in other comprehensive income are reclassified to the statement of profit or loss as a reclassification adjustment when the gain or loss on disposal is recognised.

(c) Available-for-sale fair value reserve

Available-for-sale fair value reserve represents fair value changes (net of tax) in available-for-sale financial assets.

25 Related parties and holders of 10% of the Bank’s shares

Holders of 10% or more of the Bank’s shares may include companies, individuals, or families. Families are included if the shares of the family members total 10% or more of the Bank’s shares. Members of the family of an individual are those that may be expected to influence, or be influenced by, that person in their dealings with the Bank.

Related parties also include key management personnel and HSBC Group and related entities. Details are provided separately where amounts relating to an individual director and/or significant shareholder and his/her related parties are greater than 5% of the total of related party loans and advances. Others represent transactions with parties related to more than one director.

Notes to the unaudited interim condensed financial statements (continued)

25 Related parties and holders of 10% of the Bank's shares (continued)

Analysis of the related party transactions with related parties or holders of 10% or more of the Bank's shares, ('significant shareholders') or their family members during the period is as follows:

| 30 June 2016 | Parent entity RO'000 | Other related group entities RO'000 | Directors RO'000 | Others RO'000 | Total RO'000 |
|--|---------------------------------|--|-----------------------------|--------------------------|-------------------------|
| Loans and advances | - | - | 9 | 38,111 | 38,120 |
| Current, deposit and other accounts | - | 11,153 | 74 | 9,014 | 20,241 |
| Letters of credit and guarantees | - | 77,542 | - | 7,830 | 85,372 |
| Due from banks | - | 10,732 | - | - | 10,732 |
| Due to banks | - | 13,947 | - | - | 13,947 |
| For the period ended 30 June 2016 | | | | | |
| Net fee income | - | 27 | - | - | 27 |
| Other operating expenses | - | (5,480) | (13) | (60) | (5,553) |
| Purchase of property and equipment | - | - | - | (6) | (6) |
| | Parent entity RO'000 | Other related group entities RO'000 | Directors RO'000 | Others RO'000 | Total RO'000 |
| 30 June 2015 | RO'000 | RO'000 | RO'000 | RO'000 | RO'000 |
| Loans and advances | - | - | - | 36,446 | 36,446 |
| Current, deposit and other accounts | - | 10,002 | 27 | 21,263 | 31,292 |
| Letters of credit and guarantees | - | 85,971 | - | 9,025 | 94,996 |
| Due from banks | 20,458 | 14,542 | - | - | 35,000 |
| Due to banks | 7,572 | 10,657 | - | - | 18,229 |
| For the period ended 30 June 2015 | | | | | |
| Net fee income | - | 108 | - | - | 108 |
| Other operating expenses | - | (6,080) | (10) | (107) | (6,197) |
| Other income | - | - | 9 | - | 9 |
| Purchase of property and equipment | - | - | - | (2) | (2) |

Related party loans and advances bear interest at rates between 1.45% p.a. and 6% p.a. (30 June 2015: between 1.3% p.a. and 8% p.a.). Related party deposits bear interest at rates between 0.20% p.a. and 1.25% p.a. (30 June 2015: between 0.25% p.a. and 1.25% p.a.).

Compensation of key management personnel

| | Six months ended 30 June 2016 RO'000 | Six months ended 30 June 2015 RO'000 |
|---|---|---|
| Wages, salaries and other short term benefits | 792 | 950 |
| Post-employment benefits | 122 | 223 |
| | 914 | 1,173 |

Notes to the unaudited interim condensed financial statements (continued)

26 Operating segments

The factors used to identify the Bank's reporting segment are discussed in the financial statements for the year ended 31 December 2015.

| | 30 June 2016 | | | | Total RO'000 |
|--|------------------|----------------|----------------|-----------------------|------------------|
| | CMB RO'000 | RBWM RO'000 | GB&M RO'000 | Unallocated RO'000 | |
| Net interest income | | | | | |
| - External | 9,850 | 14,472 | 2,257 | (43) | 26,536 |
| - Internal | 14 | 1,019 | (1,047) | 14 | - |
| | <u>9,864</u> | <u>15,491</u> | <u>1,210</u> | <u>(29)</u> | <u>26,536</u> |
| Net fee income | 3,860 | 2,136 | 593 | (81) | 6,508 |
| Net trading income | 1,182 | 847 | 2,090 | (5) | 4,114 |
| Other operating income | 97 | 105 | 9 | 64 | 275 |
| Total operating income | <u>15,003</u> | <u>18,579</u> | <u>3,902</u> | <u>(51)</u> | <u>37,433</u> |
| Loan impairment (charges) and other credit risk provisions - net of recoveries | (659) | (2,774) | - | - | (3,433) |
| Net operating income | <u>14,344</u> | <u>15,805</u> | <u>3,902</u> | <u>(51)</u> | <u>34,000</u> |
| Total operating expenses | (7,274) | (16,285) | (954) | (317) | (24,830) |
| Profit / (loss) before tax | <u>7,070</u> | <u>(480)</u> | <u>2,948</u> | <u>(368)</u> | <u>9,170</u> |
| Reportable segment assets | <u>965,105</u> | <u>473,523</u> | <u>702,516</u> | <u>97,588</u> | <u>2,238,732</u> |
| Reportable segment liabilities | <u>1,179,401</u> | <u>698,510</u> | <u>22,683</u> | <u>33,850</u> | <u>1,934,444</u> |

The main items reported in the unallocated category are cash in hand, fixed assets, other assets and other liabilities

| | 30 June 2015 | | | | Total RO'000 |
|--|------------------|----------------|----------------|-----------------------|------------------|
| | CMB RO'000 | RBWM RO'000 | GB&M RO'000 | Unallocated RO'000 | |
| Net interest income | | | | | |
| - External | 8,364 | 14,768 | 967 | - | 24,099 |
| - Internal | (426) | 418 | 5 | 3 | - |
| | <u>7,938</u> | <u>15,186</u> | <u>972</u> | <u>3</u> | <u>24,099</u> |
| Net fees and commission | 3,723 | 2,349 | 722 | - | 6,794 |
| Net trading income | 1,149 | 518 | 1,723 | (29) | 3,361 |
| Other operating income | 774 | 918 | 58 | 118 | 1,868 |
| Total operating income | <u>13,584</u> | <u>18,971</u> | <u>3,475</u> | <u>92</u> | <u>36,122</u> |
| Loan impairment (charges) and other credit risk provisions - net of recoveries | (568) | (1,678) | - | - | (2,246) |
| Net operating income | <u>13,016</u> | <u>17,293</u> | <u>3,475</u> | <u>92</u> | <u>33,876</u> |
| Total operating expenses | (8,717) | (17,736) | (906) | (313) | (27,672) |
| Profit / (loss) before tax | <u>4,299</u> | <u>(443)</u> | <u>2,569</u> | <u>(221)</u> | <u>6,204</u> |
| Reportable segment assets | <u>902,114</u> | <u>454,590</u> | <u>892,730</u> | <u>101,404</u> | <u>2,350,838</u> |
| Reportable segment liabilities | <u>1,210,372</u> | <u>743,730</u> | <u>61,918</u> | <u>30,914</u> | <u>2,046,934</u> |

Notes to the unaudited interim condensed financial statements (continued)

27 Capital adequacy ratio

Capital management is guided by the CBO through circular BM 1009 (Guidelines on BASEL II) and regulatory capital under BASEL III framework. Capital adequacy is calculated on quarterly intervals and reported to the CBO. The banks are required to maintain minimum capital adequacy ratio of 12.625% including capital conservation buffer for 2016 (30 June 2015 and 31 December 2015: 12.625%) in accordance with CBO stipulated guidelines.

| | 30 June 2016 RO'000 | 30 June 2015 RO'000 | 31 December 2015 RO'000 |
|---------------------------------|------------------------------------|---------------------------|-------------------------------|
| CET 1 / Tier 1 capital | 289,930 | 281,340 | 289,930 |
| Tier 2 capital (T2) | 16,682 | 17,862 | 16,682 |
| Total regulatory capital | 306,612 | 299,202 | 306,612 |
| Risk-weighted assets | 1,667,989 | 1,713,060 | 1,578,818 |
| CET 1 / Tier 1 capital ratio | 17.38% | 16.42% | 18.36% |
| Total capital ratio | 18.38% | 17.47% | 19.42% |

28 Cash and cash equivalents

| | 30 June 2016 RO'000 | 30 June 2015 RO'000 | 31 December 2015 RO'000 |
|---|------------------------------------|---------------------------|-------------------------------|
| <i>Unaudited interim condensed statement of financial position comprises:</i> | | | |
| Cash and balances with central banks | 172,974 | 336,588 | 277,736 |
| Due from banks | 49,011 | 152,972 | 10,271 |
| Due to banks | (46,254) | (49,717) | (36,211) |
| | 175,731 | 439,843 | 251,796 |
| Adjustment for items maturing after three months from date of acquisition and restricted balances | - | (15,886) | - |
| | 175,731 | 423,957 | 251,796 |
| <i>Cash and cash equivalent comprise:</i> | | | |
| Cash and balances with central banks | 172,974 | 320,702 | 277,736 |
| Due from banks | 49,011 | 152,972 | 10,271 |
| Due to banks | (46,254) | (49,717) | (36,211) |
| Total | 175,731 | 423,957 | 251,796 |

28(a) Change in operating assets

| | 30 June 2016 RO'000 | 30 June 2015 RO'000 |
|---|------------------------------------|---------------------------|
| Change in loans and advances to customers-net | (201,755) | (155,640) |
| Change in other assets | (4,336) | (1,906) |
| | (206,091) | (157,546) |

28(b) Change in operating liabilities

| | 30 June 2016 RO'000 | 30 June 2015 RO'000 |
|-----------------------------------|------------------------------------|---------------------------|
| Change in deposits from customers | 31,940 | 100,490 |
| Change other liabilities | 958 | 1,838 |
| | 32,898 | 102,328 |

Notes to the unaudited interim condensed financial statements (continued)

29 Liquidity coverage ratio (LCR)

Liquidity coverage ratio (LCR) is guided by the CBO through circular BM 1127 (BASEL III : Framework on Liquidity coverage ratio and LCR disclosure standards). Liquidity coverage ratio is calculated on monthly intervals and reported to the CBO. The Banks are required to maintain minimum liquidity coverage ratio of 70% for 2016 (for 30 June 2015 : 60%) in accordance with CBO stipulated guidelines.

Liquidity coverage ratio disclosure for the period ended 30 June 2016:

| | 30 June 2016 | | 30 June 2015 | |
|---|------------------------------------|--|------------------------------------|--|
| | Unweighted Value (average*) RO'000 | Total Weighted Value (average*) RO'000 | Unweighted Value (average*) RO'000 | Total Weighted Value (average*) RO'000 |
| High quality liquid assets | | | | |
| 1 Total High quality liquid assets (HQLA) | | 621,034 | | 700,102 |
| Cash outflows | | | | |
| Retail deposits and deposits from small business customers, of which: | | | | |
| 2 | 699,517 | 52,803 | 746,851 | 57,619 |
| 3 - Stable deposits | 342,969 | 17,148 | 341,334 | 17,067 |
| 4 - Less stable deposits | 356,549 | 35,655 | 405,517 | 40,552 |
| 5 Unsecured wholesale funding, of which: | 1,199,545 | 503,285 | 1,258,181 | 540,331 |
| - Operational deposits (all counterparties) and deposits in networks of cooperative banks | - | - | - | - |
| 6 | | | | |
| 7 - Non-operational deposits (all counterparties) | 1,199,545 | 503,285 | 1,258,181 | 540,331 |
| 8 - Unsecured debt | - | - | - | - |
| 9 Secured wholesale funding | - | - | - | - |
| 10 Additional requirements, of which | 94,418 | 9,201 | 164,261 | 16,218 |
| - Outflows related to derivative exposures and other collateral requirements | - | - | - | - |
| 11 | | | | |
| - Outflows related to loss of funding on debt products | - | - | - | - |
| 12 | | | | |
| 13 - Credit and liquidity facilities | 94,418 | 9,201 | 164,261 | 16,218 |
| 14 Other contractual funding obligations | - | - | - | - |
| 15 Other contingent funding obligations | 897,085 | 44,854 | 991,060 | 49,553 |
| 16 Total cash outflows (2+5+10+15) | | 610,143 | | 663,721 |
| Cash inflows | | | | |
| 17 Secured lending (e.g. reverse repos) | - | - | - | - |
| 18 Inflows from fully performing exposures | 197,134 | 115,764 | 304,924 | 221,986 |
| 19 Other cash inflows | - | - | - | - |
| 20 Total cash inflows (17+18+19) | 197,134 | 115,764 | 304,924 | 221,986 |
| 21 Total HQLA | | 621,034 | | 700,102 |
| 22 Total net cash outflows (16-20) | | 494,379 | | 441,735 |
| 23 Liquidity coverage ratio (21/22) | | 126% | | 158% |

*simple average of monthly observations over the last three months (Apr – Jun 2016)

30 Corresponding figures

Certain corresponding figures for 2015 have been reclassified in order to conform to the presentation for the current period. Such reclassifications have not resulted in change in prior period reported profit and equity.