

ASM - CAS. for others a validated amount copy
to read & return to Sultan

Banking Investment & Insurance

Al-Azhar Times Special Supplement

Sultanate of Oman

Basel II compliance by January 2007

Capital adequacy, one of the critical stability indicators, also improved further in banks. The sound performance, particularly in the wake of significant supervisory initiatives having implications for loans loss provisions and earnings of commercial banks, demonstrates the inherent strength of the banking system

introduction of appropriate remedial measures, fine tuning of the definition of various components of net worth, regulatory review of issues relating to connected lending, etc. in order to strengthen the financial position of licensed banks and enable them to face competition, finance large projects and increase business.

The minimum capital requirement for commercial banks was enhanced to RO50

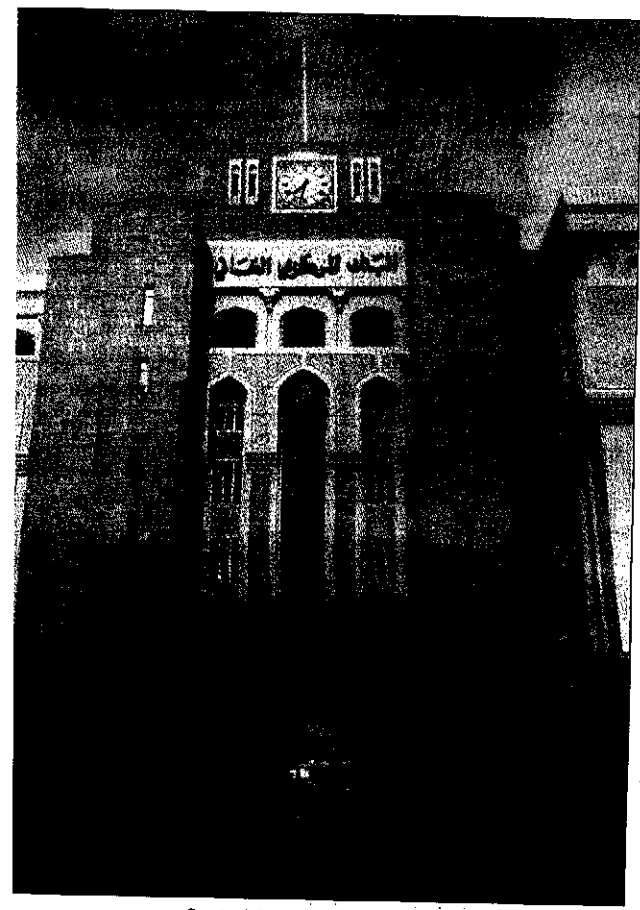
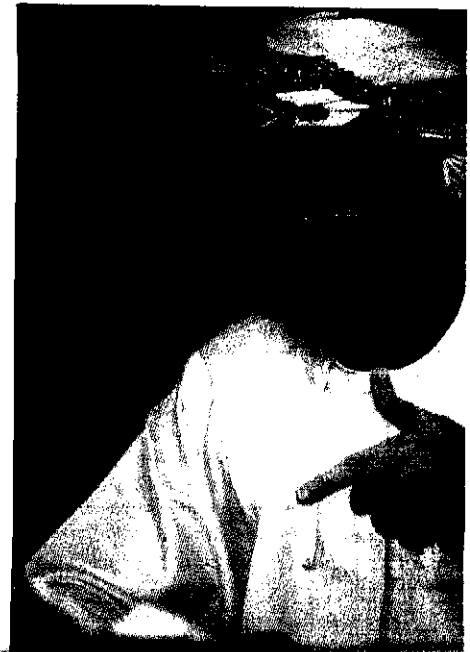
The adoption of Basel II would transform the current approaches and tools of supervision of the CBO as well as audit and risk management practices of banks. In this context, the Central Bank is contemplating to adopt risk-based supervision very shortly to supplement the objective of Basel II.

Systemically important, banks are being encouraged to plan in advance so as to remain competitive and

regulators operating in the advance financial systems. It is WTO and free Trade Agreements, banks in Oman will have to constantly upgrade their services to be able to compete globally.

Where do the non — banking finance companies stand in Oman?

Al Zadjali: there are currently six finance and leasing companies under the license of the Central Bank of Oman. They mainly operate in three



Central Bank of Oman

From January all banks in Oman will be operating under a standardised framework under the Basel II. This would transform the

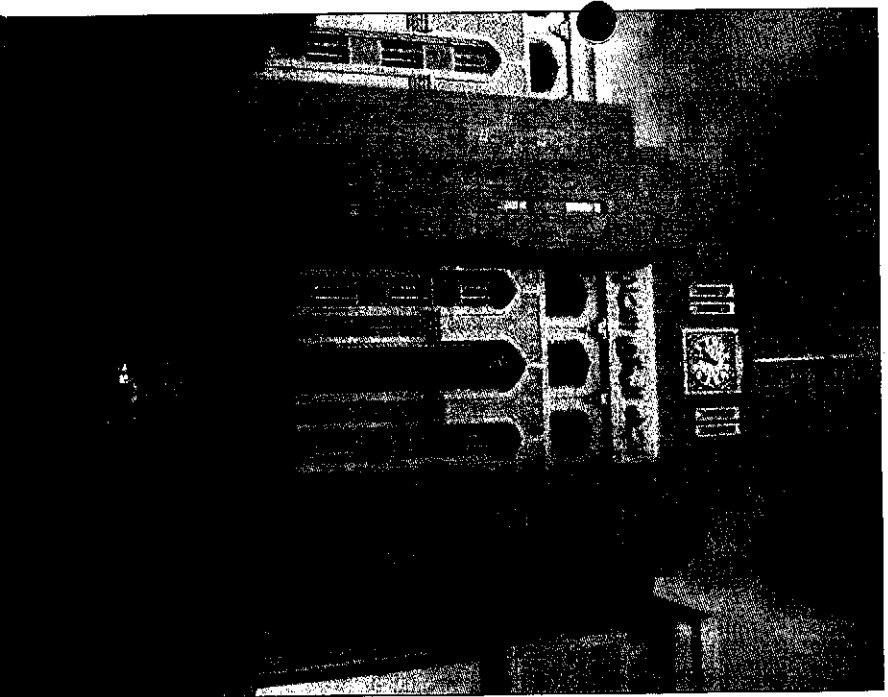
higher provision coverage supported by increasing level of profits. The total assets of commercial banks in Oman registered a growth of 15.2

ASIN - EK5
to me



Banking I

Khaleej Times Special Supplement **SU**



Central Bank of Oman

BASE II by J

Capital adequacy, one improved further in the wake of significant for loans loss provision demonstrates the inhe

higher provision coverage supported by increasing level of profits. The total assets of commercial banks in Oman registered a growth of 15.2 percent from RO4888.7 million (\$ 12.7 billion) in 2004 to RO5629.9 million (\$ 14.6 billion) as at the end of 2005.

Capital adequacy, one of the critical stability indicators, also improved further in banks. The sound performance, particularly in the wake of significant supervisory initiatives having implications for loans loss provisions and earnings of commercial banks, demonstrates the inherent strength of the banking system.

The CBO's initiatives in promoting financial stability continued during the year by putting in place a Prompt Corrective Action framework for early identification of banks in distress with the

EFFECTIVE from January 2007, all banks in Oman will be following a standardised framework under the Basel II which would transform the current approaches and tools of supervision of the Central Bank of Oman as well as audit and risk management practices of banks. The move follows on the recommendation of the group that the CBO had set up to comply with the international banking standard, said Hamoud Sangour Al Zadjali Executive President of CBO. Here are his responses to questions put up by *Khaleej Times*.
How would you rate the growth of banking industry in Oman?
Al Zadjali: The year 2005 witnessed remarkable progress in the banking sector, marked by robust growth in assets alongside significant improvement in asset quality,

introduction of appropriate prevention remedial measures, fine tuning of the definition of various components of net worth, regulatory review of issues relating to connected lending, etc. in order to strengthen the financial position of licensed banks and enable them to face competition, finance large projects and increase business.

The minimum capital requirement for commercial banks was enhanced to RO50 million for local banks and RO10 million for foreign banks. The revised off site bank monitoring system has been strengthened and is being used for identifying the supervisory concerns based on analysis of Financial Soundness Indicators.

Basel II group
The CBO had set up the Basel II implementation Group, with participation from banks, to study and recommend the course of action for implementing the new capital accord in Oman. The group has come up with its recommendations and the banking system is poised to adopt standardised framework effective from January 2007.

*Al Bishri's checked and accurate copy
of the report to Sultan*

Investment & Insurance

Sanate of Oman

JULY 5, 2006

III Compliance Summary 2007

the critical stability indicators, also
s. The sound performance, particularly in
supervisory initiatives having implications
and earnings of commercial banks,
nt strength of the banking system

The adoption of Basel II would transform the current approaches and tools of supervision of the CBO as well as audit and risk management practices of banks. In this context, the Central Bank is contemplating to adopt risk-based supervision very shortly to supplement the objective of Basel II.

Systemically important banks are being encouraged to plan in advance so as to remain competitive and sound. The CBO is constantly striving to align its risk focused supervisory framework with evolving supervisory development across various jurisdictions.

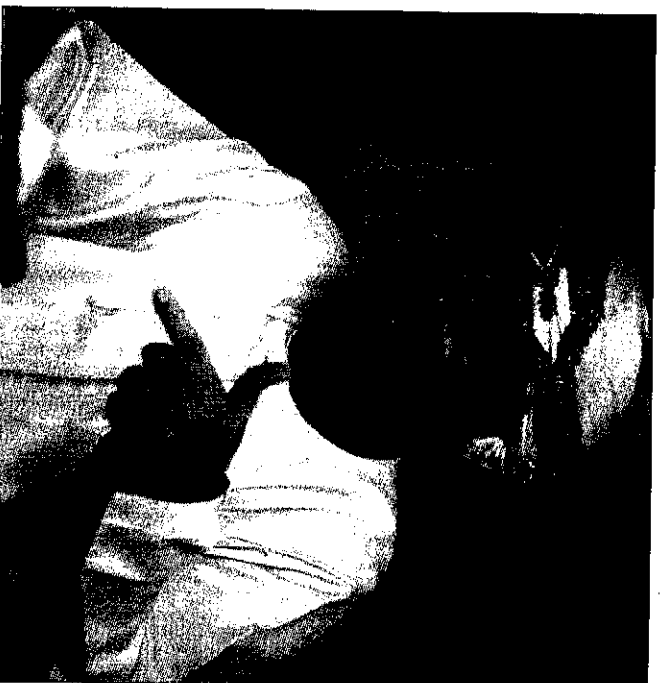
With regard to the recently signed FTA with the USA, it is felt that greater presence by the US service providers in the financial sector in this region will not only bring with it the experience, skills and technology of an advanced financial system, but would also help in recognising the need to be at par with the requirement of international best practices and standards. Cooperation between the regulatory authorities of Oman and the US will help GBO in gaining from the experience of the

regulators operating in the advance financial systems. It is WTO and free Trade Agreements, banks in Oman will have to constantly upgrade their services to be able to compete globally.

Where do the non — banking finance companies stand in Oman?

Al Zaidiati: there are currently six finance and leasing companies under the license of the Central Bank of Oman. They mainly operate in three market segments, namely, retail financing, where the financing is to individual customers mainly for automotive and electronic goods; equipment leasing, where the financial is to SME's (Small and Medium Enterprises) for expansion, modernisation and replacement requirements; factoring and working capital financing to SME's for cross border or domestic trade or for the execution of projects, usually against an assignment of receivables.

The finance and leasing sector witnessed a period of consolidation spanning the last four years. In 2004, FLCs focused on improving asset quality and enhancing their capital base to support their growth plans. Provisioning



Hamoud Sangour Al Zaidiati
Executive President of GBO

was also brought in line with the stricter provisioning norms introduced by the Central Bank.

During 2005, the leasing and finance sector continued its steady growth despite the trend of rising interest rates affecting the cost of funds and putting pressure on the margins. The retail vehicle financing industry continued to be the most competitive segment of the market. The SME equipment finance market also saw substantial growth.

Meanwhile, the FLCs continued to pursue their geographic expansion plans. New branches were opened

in the interior regions of the Sultanate, such as Ibril and Nizwa. Hence, the number of branches rose from 24 in 2004 to 27 in 2005. As FLCs entered the bancassurance business, a number of new product offerings, i.e. insurance linked products as well as non — conventional finance products, were introduced during the year.

With regard to the finances of these companies, the total combined assets of FLCs rose from RO 189 million in 2004 to RO 219.7 million in 2005. Total outstanding credit (net of provisions) extended in the

Basel II compliance by January 2007

• FROM PAGE 1

form of hire purchasing, lease financing and factoring increased to RO201.2 million in 2005 as compared to RO175.3 million in 2004, an increase of 14.8 per cent. **Is there any plan to free Omani Rial from its pegging to US Dollar?**

Al Zadjali: For an open economy like Oman, fixed peg to the US dollar works as the strongest source of stability, which is so essential for promoting trade and investment. CBO remains firmly committed to maintain the peg of the Omani Rial to the US dollar.

On the SME initiative, are there any special measures on the anvil?

Al Zadjali: The link between bank credit and a diversified private sector gets strengthened with the provision of adequate credit at competitive interest rates. The flow of credit to small and medium enterprises is of paramount importance for a diversified private sector and in particular for employment generation and for sustainable non-oil GDP growth. Banks are being encouraged to take special care towards this sector and to help in nurturing entrepreneurial talents and to ensure adequate flow of credit to small and medium enterprises.

Are you happy with the containment of inflation?

Al Zadjali: Oman has all along exhibited low and stable inflation, arising from the benefits of an open economy as well as a fixed exchange rate regime that ensures strong monetary discipline. After a period of extremely subdued domestic inflation, in 2004 there was an early sign of some increase in prices, which persisted in 2005 as well. As per the consumer price index for the sultanate, inflation rose from 0.7 per cent in 2004 to 1.9 per cent in 2005. At this level, Oman's inflation was still lower than the average inflation recorded by advanced countries in 2005.

Oman is experiencing a real estate boom. Speculative investment seems to be sizeable in this segment. How does CBO plan to check this malaise?

Al Zadjali: In Oman, real estate prices have not witnessed notable acceleration in the recent period. The uptrend seen in real estate prices in this region could be viewed in the context of (a) high economic growth and large investment in diversification project, which have created expectations of sustainable economic boom in the region, and associated expectations of higher future demand for real estate, and (b) domestic easy liquidity conditions, and the lack of alternative lucrative investment options in relation to expected return on real estate.

As a central bank, the CBO is particularly concerned about the levels of direct and indirect exposure of banks which can have determining ramifications for our goal of systemic financial stability. Our prudential regulations clearly reflect our concerns, even though we do encourage bank lending for residential housing, which is viewed by us a basic need and hence covered under personal loans.

As per CBO's recently modified policy on quantitative ceiling for personal loans, banks have been allowed to lend exclusively for residential housing up to 5 per cent of their total credit. Banks are expected to better recognise and manage the risk associated with commercial real estate and indirect real estate exposures arising from the possibility of sudden cyclical declines in real estate prices.