MORTGAGE AND LAND BANK OF LATVIA

Annual Report for the year ended 31 December 2009

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V a/s „Latvijas Hipotēku un zemes banka" (Bank) is a joint-stock company incorporated in the Republic of Latvia. The holder of 100% of the Bank's shares is the Ministry of Finance of the Republic of Latvia. The Bank and its subsidiaries (the Group) are engaged in banking and financial services business.

Report of the Supervisory Council and the Board of Directors

The year 2009 has been a year of significant decisions and development for the SJSC "Mortgage and Land bank of Latvia". With the concept on transformation of the Mortgage bank into a development bank, approved by the Cabinet of Ministers, another significant step has been made last year into the direction of the formation of the development bank, so essential for the state of Latvia.

Under the tough present economic conditions, the Mortgage bank continued lending to Latvian enterprises within industries essential for the national economy as determined by the state, augmenting the range of traditional services offered by the commercial banks. An essential fact is that the proportion of state aid framework programmes in the total portfolio of the Mortgage bank has grown from 12 to 39% in 2009. With the risk of granted loans rising as a result of the influence of the overall economic situation, the Mortgage bank in 2009 has built provisions for doubtful assets of 74.2 million lats, while the equity capital of the bank has been increased by 72.8 million lats. In last year, the Mortgage bank also repaid a considerable amount of syndicated loans and accrued funds for of next loan repayment.

We can boast an increase of the number of clients in the Mortgage bank both in sectors of legal entities and private individuals under the conditions of economic recession. The volume of term deposits has also grown, as well as the Mortgage bank's market share in the deposits sector, which indicates a high level of client loyalty for the bank.

We are going to proceed in increasing the implementation volumes of promotional programmes further in 2010, financing entrepreneurs and stimulating the development of the Latvian national economy. We are also going to further improve the quality of the bank's services and maintain high standard of customer service.

Global economic situation and its stabilization prospective

The International Monetary Fund estimates that the global economy in 2009 might have decreased by 1.1%, but in 2010 the world's economy might grow by 3.1%. After the deep recession of the global economy the economic growth has become positive, as the extensive measures implemented by countries have contributed to demand and reduced the uncertainty and the probability of systemic risks occurrence on financial markets.

The IMF forecasts that the economies of European development countries would grow by 1.8% in 2010, compared to the 5.0% drop in 2009.

A quarterly decline of the Gross National Product (GDP) by 16.8% was registered in the 4th quarter of 2009 in Latvia (data of the Central Bureau of Statistics), indicating the proximity of the economy to its lowest point. Reduction of the GDP by 2-4% in 2010 is forecasted.

The factors, most closely related to the decrease of economic activity, are:

- decline in dominant industries of economy, which saw the greatest upsurge in previous years and are internal demand oriented: retail, construction, financial services, tourism, catering services etc.;
- drop of industrial output in 2009 compared to 2008 by 16.1%;
- the material reduction of Latvian national budget expenditures and rise in tax rates that will mark further decrease of the domestic demand also in 2010;
- unemployment level, that reached 16% in December of 2009 (in December of the previous year – 7%). The unemployment level might reach 20% in the first half of 2010, though the employment growth might restart only with resumption of economy growth, expected to occur in the second half of 2010;
- amassing of risks in the financial system of Latvia – the volume of non-performing loans on the rise, doubtful loans require building of provisions, substantial losses of banking operations, as well as the necessity to repay external loans. Credit resources have also become substantially more expensive. Thus the credit resources available to economy keep decreasing.

There are several factors indicating a stabilization and formation of preconditions for a balanced development of economy in the future:

- stabilization of exports ratios – dynamics of exports structure in major groups of goods by months indicate that, after a significant drop of export in 2008, 2009 brings the first early signs of rehabilitation. With economic growth resuming the swing in other countries of the European Union, being the primary export market for Latvia, a gradual increase of exports may be expected, which would allow the Latvian economy to recover. Where until now the ratio of exports to GDP has been within boundaries of 35-45%, then, with industries of domestic demand diminishing due to the restructuring of economy, in 2010 exports might already seize the dominant position in economy, exceeding 50% of the GDP;
- improvement of foreign trade, greatly affected by the traditionally stabile balance of services trading, as well as rapid fall of imports, with the internal consumption shrinking;

Report of the Supervisory Council and the Board of Directors *(continued)*

- improvement of Latvia's balance of payments – the balance of the current account has been positive through all months of 2009. Current account surplus might be expected also further on, though it may fluctuate depending on losses of direct investment companies, reflecting as positive revenues account;
- halt of inflation growth and stabilization of consumer prices. Annual deflation was registered in October, for the first time in the history of the re-established Latvia. In December of 2009 if compared to December of 2008, consumer prices shrunk by 1.2%. The limited purchasing capacity of consumers will be the major driver for prices to drop further on. Therefore the deflation will continue throughout 2010, the contraction of prices hanging on the level of 3-5% by annual profile;
- reduction of labour force costs, substantially affected by unemployment growth and zooming supply of free hands. This circumstance will have a propulsive effect on the competitiveness of Latvian enterprises on the international market;
- actual effective rates of the lats approaching the nominal rates.

Financial sector and its tendencies

On 31 December 2009, the banking services in Latvia are provided by 21 banks and six branches of foreign banks. The SJSC "Mortgage and Land bank of Latvia" is operating as the only 100% state-owned commercial bank.

In 2009, by unaudited data, the assets of the banks operating in Latvia have decreased by 7%, reaching 21.7 billion lats at the end of December, the volume of the loan portfolio decreased by 7%, deposits (including the transit funds) – by 2%, and the capital and reserves of the banks – by 6%. In 2009, the unaudited losses of banks reached 773 million lats mostly due to accumulation of provisions for non-performing loans.

The lending of banks to the private sector still receded, driven by the cautious lending policies of banks due to the complex economic situation, as well as the low demand in households sector as well as the sector of non-finance companies. But for all that, the total drop of the lending volume (by 7%) may not be regarded as steep, considering the high level of risk in economy and the necessity of banks to build provisions and restructure loans.

The credit resources available to Latvian commercial banks on the financial market substantially shrunk in 2009, along with the capacities of banks to refinance long-term interbank borrowings, and reduction of deposits also diminished the supply of money. Although euro deposits in 2009 have increased, the deposits in lats and US dollars have considerably dropped.

The decreasing growth of Latvian economy and price increase of credit resources has affected the loan portfolio quality of Latvian commercial banks, which has considerably deteriorated over the last year. At the end of 2009, the performing (non-overdue) loan portfolio of the banking sector reached 74.5%. Recovery options of problem loans are becoming more and more complicated, as a result of which the volume of write-off loans in the financial sector is growing.

The reserve requirements imposed by the Bank of Latvia have not changed in 2009: for bank liabilities exceeding 2 years – 3%, for all other liabilities included in the reserve base – 5%.

The US Federal Reserve system has maintained the dollar basic interest rate at its historically lowest mark during 2009 (0.25%). the European Central Bank reduced the euro basic interest rate – from 2.5% to 1.0%, and the Bank of Latvia has also reduced the lats basic interest rate from 6% to 4%, as a result of which this period saw a decrease of the average interest rate for loans issued by Latvian commercial banks. The average interest rate for private borrowers (in lats) decreased from 17.48% (December 2008) to 12.15% (December 2009), while for legal entities the decrease for the corresponding period was from 13.44% to 6.74%. The average interest rates for legal entities (in foreign currencies) decreased from 6.72% (December 2008) to 4.20% (December 2009), and for private borrowers – from 7.48% to 5.79%. In light of the activities of foreign central banks, targeted to boost the economies, interest rates for loans in foreign currencies would still remain lower than the rates for loans in lats, an essential factor for clients when selecting the loan currency.

Financial results

To the contrary of the trend in the banking sector, the volume of gross assets of the Mortgage Bank in 2009 increased by 4.4 million lats reaching 967 million lats (market share – 4.5%). Due to the global deterioration of the economic situation, with the risk of granted loans rising, Mortgage bank has accumulated the provisions for doubtful assets in the amount of 74.2 million lats during 2009.

Report of the Supervisory Council and the Board of Directors *(continued)*

The losses of the Bank for 2009 were 54.1 million lats, and the retained earnings of the bank for previous years were 12 million lats.

In 2009, the gross loans' portfolio of the Mortgage Bank has decreased by 24.1 million lats or 3%, reaching 707.5 million lats (market share – 4.6%).

The volume of deposits (including the transit funds) with the Mortgage Bank in 2009 has increased by 22.3 million lats or by 8% to 326.8 million lats (market share – 3.4%).

The Bank in 2009 repaid syndicated loans and other interbank long-term loans of 215.2 million euro (151.3 million lats). In 2010, syndicated and other interbank long-term loans will be defrayed by 149 million lats.

In January 2009 the equity capital of the Bank was increased by 29.5 million lats. On 20 November 2009, the shareholder of the Mortgage Bank upon approval from the European Commission (decision no. NN60/2009) increased the equity capital of the Bank by 43.29 million lats. Thus the total volume of the paid-up share capital reached 121.32 million lats. The capital adequacy ratio of the Bank was 12.8% on 31.12.2009, which considerably exceeds the statutory minimum of 8% as directed by the Law on Credit Institutions.

Increase of the equity capital of the Mortgage Bank was included in the law on 2010 national budget (Article 12). Pursuant to that, the equity capital of the bank is to be increased by 70.2 million lats, with the state taking over liabilities of the Mortgage bank towards the Nordic Investment bank (NIB) and investing the respective amount into the equity capital of the bank. The recapitalization shall be conducted at the end of 1st quarter of 2010 according to the Bank's action plan. These funds shall be used for lending under the Programme for improvement of competitiveness of businesses. It means that these funds will remain with the bank after repayment of the granted loans, and the Mortgage bank would further use them for funding of Latvian entrepreneurs under the Programme for improvement of competitiveness of businesses.

In February 2009 the Mortgage Bank and Privatisation Agency concluded a share purchase agreement for the sale of the shares of Parex Bank by Mortgage Bank to Privatisation Agency.

At the beginning of 2009 the international rating agencies started gradual downgrade of the credit ratings of Latvia. *Standard & Poor's Rating Services* and *Fitch Ratings* downgraded Latvia's sovereign credit ratings to BB and BB+ respectively that was a speculative rating, noting that the downgrading reflected the worsening of the economic situation faster than anticipated. *Moody's Investors Service Ltd* downgraded the sovereign rating on Latvia to the lowest investment grade rating *Baa3*. The Mortgage Bank is 100% owned by state and its rating may not exceed Latvia's sovereign rating. For this reason *Moody's Investors Service Ltd* lowered the credit ratings of the Mortgage Bank along with the downgrading of the sovereign rating. The Bank is assigned the following ratings:

- long-term foreign currency deposits – ***Baa3***,
- short-term foreign currency deposits – ***P3***,
- financial strength rating – ***E+***,
- rating of mortgage bonds – ***Baa2***,

which are investment grade ratings.

At the end of 2009, the Mortgage Bank serviced its clients in 27 branch offices, located in Riga as well as in each district centre of Latvia, and 8 sub-branches in various regions of the country. While maintaining the mission to provide banking services to the population as accessible and convenient as possible, the Mortgage Bank conducted optimization of the bank's branch and sub-branch network in 2009: the status of Valka branch and Smiltene sub-branch were changed, Sigulda sub-branch of Ūnija branch and the sub-branch of Liepāja branch were closed, while Balvi and Ludza branches were transformed into sub-branches. These reorganizations allowed to achieve higher efficiency and reduce costs.

We are happy to declare that Preiļi Branch office was among the top ten most praised places of good service in the Pan-Latvian campaign "Praise good service!".

Proceeding with expansion of its ATM network, the Mortgage Bank installed 17 new ATMs in 2009, with the total ATM network of the Mortgage Bank thus expanding to 72 ATMs. The customers of Mortgage Bank can withdraw cash without commission fee being applied also in the network of "friendly ATMs" (Rietumu banka, Latvia Krājbanka, SEB banka, Parex banka), the total of 633 ATMs across Latvia.

Report of the Supervisory Council and the Board of Directors *(continued)*

Course of development bank operations, implementation of state aid programmes

On 3 December 2009, the concept "Transformation of the "State Joint-stock company "Mortgage and Land bank of Latvia" into Development bank" was accepted by the Cabinet of Ministers decree No.820. The goal of the concept was to select the optimum options for transformation of the Mortgage bank into development bank, by reducing transactions of commercial bank and channelling the bank's operations into directions currently crucial for the national economy.

In line with the decided by the Cabinet of Ministers, favour was granted to the concept model, encompassing formation of the development bank on the fundaments of the Mortgage bank and gradual phasing out of commercial banking functions until the deadline of 31 December 2013. According to the favoured model of the concept, the bank continues implementation of the existing state aid programmes, in cooperation with line ministries develops new promotional programmes, the start of implementation of which is decided by the Government.

The Mortgage bank gradually reduces the volume of the bank's commercial loan portfolio. In the area of commercial activity, the bank has already stopped lending to new clients and grants commercial loans only to existing clients, according to the present loan volume, and for restructuring of the existing loans of the bank's current commercial clients.

The Mortgage bank in 2009 continued implementation of promotional programmes, where aid is provided to certain groups of entrepreneurs and population as tasked by the government:

- Programme for improvement of the competitiveness of businesses;
- Microlending programme;
- Start programme "Support to Self-employment and Business Start-ups".

Programme for improvement of the competitiveness of businesses

On 17 February 2009, with the aim to boost entrepreneurship in Latvia, the Cabinet of Ministers passed Regulations No. 164 on lending to improve the competitiveness of businesses. As directed by these Regulations, the Mortgage Bank shall grant investment and working capital loans to small, medium and large entrepreneurs. In May, the Mortgage Bank received the first 50 million euro (35.1 million lats) for implementation of this programme from the Nordic Investment Bank (NIB), and the remaining 50 million euro (35.1 million lats) got transferred in July.

On 10 March 2009, the Cabinet adopted regulations No 238 regarding Activity 2.2.1.4 "Loans for Improvement of Competitiveness of Businesses" of the Supplement of Action Programme "Business and Innovations" that prescribe establishment of the Loan Fund as a separate financial resources unit in the Mortgage Bank for lending to the entrepreneurs under Cabinet Regulations No 164 (regarding loans for raising of competitiveness of businesses). The Loan Fund consists of the public financing in the amount of 61.6 million euro (43.3 million lats) and financing of the Mortgage Bank – 21.6 million euro (15.2 million lats). Lending from the Loan Fund was initiated in May of this year. 101.6 million lats had been granted under the competitiveness improvement programme by the end of December 2009, including 29.5 million lats from the Loan Fund.

Microlending programme

In the first quarter of this year, in accordance with the Cabinet Decree No 752 dated 2 December 2008, the Mortgage Bank commenced implementation of the Small and Medium Enterprises Microlending Programme granting microloans up to 3 thousand lats. The total financing volume of the programme is 564.8 thousand lats. By the end of December, the Mortgage Bank had granted microloans for the total amount of 404 thousand lats.

Programme "Support to Self-employment and Business Start-ups"

In compliance with the Cabinet of Ministers Regulations No 293, passed on 31 March 2009, "On Action Programme "Human Resources and Employment" supplement 1.3.1.2. activity "Support to Self-employment and Business Start-ups"", in August the Mortgage Bank initiated implementation of the Start programme, which provides training in business fundaments to business start-ups as well as consultations in preparing a business plan. In case of a positive decision of a lending committee, the participant of the programme receives a loan and grants for implementation of the project described in the business plan. By the end of December, 483 applicants had applied for consultations and training and training was started at the end of December; 106 business plans had been submitted to the bank, 51 of which was considered in credit committee and 29 were granted loans in the total amount of 565 thsd LVL and grants of 133 thsd LVL.

Report of the Supervisory Council and the Board of Directors *(continued)*

In 2010, the Bank is planning to launch an SME growth lending programme to stimulate the development of micro, small and medium entrepreneurs and farmers' unions in accordance with the Cabinet of Ministers regulations No.1065 of 15.09.2009. The aim of the programme is to improve the access to funding of entrepreneurs registered in Latvia, to revive and stimulate the development of Latvian national economy. For implementation of the programme, the Mortgage bank has signed a 100 million euro loan agreement with the European Investment bank on 2 October 2009, which will become valid after the state guarantee agreement is signed.

Nourishing the traditions launched in previous years, the Mortgage Bank closely cooperates with Latvian regions – in spring of 2009 the Bank signed co-operation agreements with the leaders of all five regional funds established in Latvia (funds of Valmiera, Talsi, Alūksne, Liepāja and Lielvārde), as well as councils of Limbaži, Ogre and Ērgļi regions, and Jūrkalne parish council on organisation of project tender. The Bank supports the best projects promoting activity and self-initiative of the local population in improving their surrounding environment submitted to tenders organized by the funds. 129 projects got implemented in cooperation with the Regional funds. Meanwhile, in cooperation with the Riga Technical University, the project "Good practice" was organized, providing students of engineering sciences with one-month of field practice during summer in client companies of the Mortgage Bank and other industry leaders in Latvia.

Baiba Bāne	Rolands Paņko
Chairman of the Council	Chairman of the Board

As at 31 December 2009 and as at the date of signing the accounts:

Supervisory Council (at 31 December 2009)

Baiba Bāne	Chairman of the Council
Dāvids Tauriņš	Deputy Chairman of the Council
Baiba Brigmane	Member of the Council

During the reporting period Jānis Šnore, Matīss Markuss and Iveta Strautiņa resigned from the Council and Baiba Brigmane was appointed as member of the Council.

Board of Directors (at 31 December 2009)

Rolands Paņko	Chairman of the Board
Jēkabs Krieviņš	Deputy Chairman of the Board
Andris Riekstiņš	Member of the Board
Jānis Bērziņš	Member of the Board

During the reporting period Inesis Feiferis resigned from the Board and Rolands Paņko has been elected as the Chairman of the Board, Jēkabs Krieviņš has been elected as the Deputy Chairman of the Board.

During the reporting period Aija Laicāne resigned from the Board and Jānis Bērziņš was appointed as the Member of the Board.

Supervisory Council (from 1 March 2010)

Baiba Bāne	Chairman of the Council
Dāvids Tauriņš	Deputy Chairman of the Council
Jānis Pone	Member of the Council

During the reporting period Baiba Brigmane resigned from the Council and Jānis Pone was appointed as the Member of the Council.

Board of Directors (from 12 March 2010)

Rolands Paņko	Chairman of the Board
Jēkabs Krieviņš	Deputy Chairman of the Board
Jānis Bērziņš	Member of the Board
Baiba Brigmane	Member of the Board
Gints Āboltiņš	Member of the Board

After the reporting period Andris Riekstiņš resigned from the Board and Baiba Brigmane and Gints Āboltiņš were appointed as the members of the Board.

Statement of Responsibility of the Supervisory Council and the Board of Directors

Riga 17 March 2010

The Supervisory Council and the Board of Directors (Management) are responsible for preparing the financial statements from the books of prime entry of the Group and the Bank for each financial period that present fairly the state of affairs of the Group and the Bank as at the end of the financial period and the results of their operations and cash flows for that period according to the International Financial Reporting Standards as adopted by the European Union. Prudent and reasonable judgments and estimates have been made by the Management in the preparation of the financial statements.

Management confirms that suitable accounting policies have been used and applied consistently and reasonable and prudent judgments and estimates have been made in the preparation of the financial statements on pages 10 to 70 for 2009. Management also confirms that applicable International Financial Reporting Standards as adopted in EU have been used in preparation of the financial statements and that these financial statements have been prepared on a going concern basis. Appropriate accounting policies have been applied on a consistent basis.

Management is responsible for keeping proper accounting records, for taking reasonable steps to safeguard the assets of the Group and the Bank and to prevent and detect fraud and other irregularities. Management is also responsible for managing the Bank in compliance with the Law on Credit Institutions, regulations of the Bank of Latvia and the Financial and Capital Market Commission as well as other legislation of the Republic of Latvia.

On behalf of the management,

Baiba Bāne
Chairman of the Council

Rolands Paņko
Chairman of the Board

PRICEWATERHOUSECOOPERS

INDEPENDENT AUDITORS' REPORT

To the Shareholders of JSC Mortgage and Land Bank of Latvia

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of JSC Mortgage and Land Bank of Latvia and its subsidiaries (the Group) and the financial statements of JSC Mortgage and Land Bank of Latvia (the Bank) on pages 10 to 70 which comprise the statement of financial position as of 31 December 2009 and the statements of income, comprehensive income, changes in shareholder's equity and cash flows for the year then ended and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements
Management is responsible for the preparation and fair presentation of these financial statements in accordance with the International Financial Reporting Standards as adopted by the European Union. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

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

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

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

Opinion
In our opinion, the accompanying financial statements give a true and fair view of the financial position of the Group and the Bank as of 31 December 2009, and of their financial performance and their cash flows for the year then ended in accordance with the International Financial Reporting Standards as adopted by the European Union.

Report on Other Legal and Regulatory Requirements
We have read the Management Report set out on pages 2 to 6 and did not identify material inconsistencies between the financial information contained in the Management Report and that contained in the financial statements for 2009.

PricewaterhouseCoopers SIA
Certified audit company
Licence No. 5

Ahmed Abu Sharkh
Chairman of the Board

Ilandra Lejiņa
Certified auditor in charge
Certificate No. 168

Riga, Latvia
17 March 2010

INCOME STATEMENT (all amounts in thousands of Euro)

	Notes	2009		2008	
		Group	**Bank**	**Group**	**Bank**
Interest income	5	78,219	75,406	94,060	90,417
Interest expense	6	(43,326)	(42,744)	(63,937)	(62,697)
Net interest income		**34,893**	**32,662**	**30,123**	**27,720**
Provision for impairment losses	13	(107,573)	(105,604)	(13,204)	(12,158)
Net interest (loss) / income after provision for impairment losses		**(72,680)**	**(72,942)**	**16,919**	**15,562**
Fee and commission income	7	6,047	5,570	5,821	5,700
Fee and commission expense	8	(1,417)	(1,458)	(1,419)	(1,383)
Net fee and commission income		**4,630**	**4,112**	**4,402**	**4,317**
Dividend income		7	74	18	1,157
Net trading income	9	8,773	8,991	3,068	3,107
Other operating income	10	9,383	7,196	6,783	4,894
Staff costs	11	(13,695)	(12,198)	(14,368)	(12,798)
Administrative and other operating expenses	12	(12,268)	(10,962)	(13,020)	(11,545)
Depreciation and amortisation		(2,897)	(2,610)	(3,325)	(2,877)
Profit before income tax		**(78,747)**	**(78,339)**	**477**	**1,817**
Income tax expense	14	1,329	1,431	(219)	(100)
Net (loss) / profit for the period		**(77,418)**	**(76,908)**	**258**	**1,717**
Attributable to:					
Equity holders of the Bank		(77,434)	-	255	-
Minority interest		16	-	3	-

Statement of Comprehensive Income (all amounts in thousands of Euro)

		2009		2008	
		Group	**Bank**	**Group**	**Bank**
(Loss) / Profit for the period		**(77,418)**	**(76,908)**	**258**	**1,717**
Net loss from investment securities available-for-sale	39	751	751	(2,877)	(2,877)
Total comprehensive loss for the period		**(76,667)**	**(76,157)**	**(2,619)**	**(1,160)**

The notes on pages 15 to 70 are an integral part of these financial statements.

These financial statements on pages 10 to 70 have been accepted by the Board of Directors on 9 March 2010 and accepted by the Supervisory Council on 17 March 2010 and are signed by:

Baiba Bāne
Chairman of the Council

Rolands Paņko
Chairman of the Board

STATEMENT OF FINANCIAL POSITION
(all amounts in thousands of Euro)

	Notes	31/12/09		31/12/08	
Assets		**Group**	**Bank**	**Group**	**Bank**
Cash and balances with Central Bank	15	136,591	136,591	64,193	64,193
Trading securities	16	7,220	6,999	5,491	5,280
Investment securities – held to maturity	16	61,161	61,161	91,163	91,020
Investment securities – available for sale	16	70,990	70,990	37,416	37,416
Due from credit institutions	18	50,385	50,193	93,322	92,962
Derivative financial instruments	19	2,780	2,780	2,250	2,250
Loans to customers	20	900,224	909,928	1,056,320	1,033,823
Investment properties	17	1,659	1,659	2,598	2,598
Investments in subsidiaries and associated undertakings	21	398	2,174	421	1,278
Intangible assets	22	3,136	2,449	3,463	2,763
Property and equipment	23	10,723	9,812	12,389	10,868
Current income tax assets		-	-	1,632	1,429
Other assets	24	12,658	2,654	7,114	2,071
Deferred expenses and accrued income		942	757	1,022	802
Total assets		**1,258,867**	**1,258,147**	**1,378,794**	**1,348,753**
Liabilities					
Due to credit institutions	25	539,997	539,997	733,103	705,641
Due to customers	26	462,076	462,164	429,847	430,005
Derivative financial instruments	19	221	221	777	777
Transit funds		2,775	2,775	3,238	3,238
Issued debt securities	27	53,257	54,423	57,854	57,854
Other liabilities	29	38,986	38,182	18,616	17,613
Deferred income and accrued expenses		5,687	4,804	3,714	2,678
Current income tax liabilities		61	-	-	-
Deferred tax liabilities	28	38	-	1,431	1,431
Subordinated liabilities	30	44,236	44,236	44,236	44,236
Total liabilities		**1,147,334**	**1,146,802**	**1,292,816**	**1,263,473**
Shareholder's equity					
Share capital	31	172,624	172,624	69,028	69,028
Reserve capital		3,591	2,935	3,591	2,935
Minority interest		57	-	41	-
Revaluation deficit on available for sale investments		(4,317)	(4,317)	(5,068)	(5,068)
(Accumulated loss) / retained earnings		(60,422)	(59,897)	18,386	18,385
Total shareholder's equity		**111,533**	**111,345**	**85,978**	**85,280**
Total liabilities and shareholder's equity		**1,258,867**	**1,258,147**	**1,378,794**	**1,348,753**
Off balance sheet items					
Contingent liabilities	35	17,188	20,196	34,159	34,159
Financial commitments	35	46,865	78,726	42,325	56,060

The notes on pages 15 to 70 are an integral part of these financial statements.

These financial statements on pages 10 to 70 have been accepted by the Board of Directors on 9 March 2010 and accepted by the Supervisory Council on 17 March 2010 and are signed by:

Baiba Bāne
Chairman of the Council

Rolands Paņko
Chairman of the Board

CONSOLIDATED STATEMENT OF CHANGES IN THE GROUP'S EQUITY
(all amounts in thousands of Euro)

	Attributable to equity holders					
	Share Capital	**Reserve capital**	**Revaluation deficit on available for sale investments**	**Retained Earnings / (accumulated loss)**	**Minority interest**	**Total equity**
Balance as at 31 December 2007	**69,028**	**3,591**	**(2,191)**	**20,492**	**-**	**90,920**
Distribution of profit – payment for use of state capital	-	-	-	(2,361)	-	**(2,361)**
Minority share of IPAS „Hipo fondi" on the date of acquisition	-	-	-	-	38	**38**
Net loss on available for sale investments	-	-	(2,877)	-	-	**(2,877)**
Profit for the year	-	-	-	255	3	**258**
Balance as at 31 December 2008	**69,028**	**3,591**	**(5,068)**	**18,386**	**41**	**85,978**
Distribution of profit – payment for use of state capital	-	-	-	(1,374)	-	**(1,374)**
Net profit on available for sale investments	-	-	751	-	-	**751**
Shareholders cash contribution (see Note 31)	103,596	-	-	-	**-**	**103,596**
Loss for the year	-	-	-	(77,434)	16	**(77,418)**
Balance as at 31 December 2009	**172,624**	**3,591**	**(4,317)**	**(60,422)**	**57**	**111,533**

The notes on pages 15 to 70 are an integral part of these financial statements.

STATEMENT OF CHANGES IN THE BANK'S EQUITY
(all amounts in thousands of Euro)

	Share Capital	Reserve capital	Revaluation deficit on available for sale investments	Retained Earnings / (accumulated loss)	Total equity
Balance as at 31 December 2007	**69,028**	**2,935**	**(2,191)**	**19,028**	**88,800**
Distribution of profit – payment for use of state capital	-	-	-	(2,360)	**(2,360)**
Net loss on available for sale investments	-	-	(2,877)	-	**(2,877)**
Profit for the year	-	-	-	1,717	**1,717**
Balance as at 31 December 2008	**69,028**	**2,935**	**(5,068)**	**18,385**	**85,280**
Distribution of profit – payment for use of state capital	-	-	-	(1,374)	**(1,374)**
Net profit on available for sale investments	-	-	751	-	**751**
Shareholders cash contribution (see Note 31)	103,596	-	-	-	**103,596**
Loss for the year	-	-	-	(76,908)	**(76,908)**
Balance as at 31 December 2009	**172,624**	**2,935**	**(4,317)**	**(59,897)**	**111,345**

The notes on pages 15 to 70 are an integral part of these financial statements.

STATEMENT OF CASH FLOWS
(all amounts in thousands of Euro)

	2009		2008	
	Group	**Bank**	**Group**	**Bank**
Cash flows from operating activities				
(Loss) / profit before taxation	(78,747)	(78,339)	477	1,817
Depreciation and amortisation	2,897	2,610	3,325	2,877
Increase in provision for impairment losses	94,446	92,921	10,309	9,506
(Profit) / loss from sale of property and equipment	(598)	115	(139)	(1)
Increase in deferred income and accrued expenses	1,974	2,126	997	746
Decrease in deferred expenses and accrued income	80	45	132	178
(Increase) / decrease in other assets	(3,344)	1,724	(8,401)	(6,669)
Increase in other liabilities	19,815	20,013	2,186	2,254
Increase in cash and cash equivalents from operating activities before changes in assets and liabilities	**36,523**	**41,215**	**8,886**	**10,708**
Decrease / (increase) in balances due from credit institutions	40,575	40,575	(13,261)	(13,261)
Decrease / (increase) in loans to customers	64,783	32,877	(113,520)	(101,089)
Decrease in trading securities	(1,753)	(1,719)	(840)	(629)
(Decrease) / increase in balances due to credit institutions	(200,725)	(173,726)	18,782	3,783
Increase in balances due to customers	32,229	32,160	28,420	27,972
Decrease in transit funds	(464)	(464)	(425)	(425)
Decrease in debt securities issued	(4,597)	(3,431)	(16,838)	(16,838)
Cash and cash equivalents used in operating activities	**(33,429)**	**(32,513)**	**(88,796)**	**(89,779)**
Corporate income tax paid	**(3)**	**-**	**(1,476)**	**(1,026)**
Cash flows from investing activities				
Increase in investment securities	(6,088)	(6,232)	(35,616)	(35,474)
Purchases of property and equipment	(1,574)	(1,386)	(3,914)	(2,517)
Proceeds from property and equipment disposal	1,268	31	518	60
Proceeds from disposal of investments in associated entities	23	-	386	34
Acquisition of investments in associated entities	-	(1,231)	(21)	-
Cash and cash equivalents used in investing activities	**(6,371)**	**(8,818)**	**(38,647)**	**(37,897)**
Cash flows from financing activities				
Shareholders cash contribution	103,596	103,596	-	-
Proceeds from subordinated liabilities	-	-	30,000	30,000
Subordinated liabilities repaid	-	-	(4,695)	(4,695)
Dividend paid	(1,374)	(1,374)	(2,361)	(2,361)
Cash and cash equivalents generated from financing activities	**102,222**	**102,222**	**22,944**	**22,944**
Increase / (decrease) in cash and cash equivalents	**62,418**	**62 122**	**(105,975)**	**(105,758)**
Cash and cash equivalents at the beginning of the year	81,753	81 856	187,728	187,616
Cash and cash equivalents at the end of the year (see Note 32)	**144,171**	**143 978**	**81,753**	**81,858**

The notes on pages 15 to 70 are an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

1 GENERAL INFORMATION

The Mortgage and Land Bank of Latvia was established as a state-owned commercial bank on 19 March 1993 by the Government of Latvia based on the Decree No 140 adopted by the Cabinet of Ministers. The Bank was registered with the Register of Enterprises of the Republic of Latvia on 3 June 1993. According to the Commercial Law the Bank was registered in the Commercial Register on 14 July 2004.

The operations of the Bank are regulated by the law On Credit Institutions and other effective laws of the Republic of Latvia, the Statutes of the Bank, the instructions of the Bank of Latvia and Financial and Capital Market Commission, as well as the decrees and regulations of the Cabinet of Ministers of the Republic of Latvia. The Bank is under the jurisdiction of the Ministry of Finance of the Republic of Latvia that represents the interests of the shareholder on behalf of the Cabinet of Ministers and holds 100% of the Bank's shares.

These financial statements on pages 10 to 70 have been accepted by the Board of Directors on 9 March 2010 and accepted by the Supervisory Council on 17 March 2010.

2 ACCOUNTING POLICIES

(1) Basis of preparation

These financial statements are prepared in accordance with International Financial Reporting Standards (IFRS) as adopted in the European Union, on a going concern basis. In preparation of the financial statements on a going concern basis the management considered the Bank's and the Group's financial position, access to financial resources and analysed the impact of the recent financial crisis on future operations of the Bank and the Group The financial statements are prepared under the historical cost convention as modified by the fair valuation of financial assets held as available-for-sale, trading securities, derivative financial instruments and investment properties.

The preparation of financial statements in accordance with EU International Financial Reporting Standards requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on the Management's best knowledge of current events and actions, actual results ultimately may differ from those estimates.

Instability in the global and Latvian financial markets and economies

Along with changes caused by the economic and financial crisis since 2008, among other things, financial markets have experienced material changes in the form of diminishing financial assets and increasing financing costs, and uncertainty in the business and investment environment has increased. Changes in the global financial markets have caused banks and other financial institutions to go bankrupt, with bank rescues being undertaken in many countries including Latvia. Although the recovery trend is strengthening in the global economy, it is currently not possible to predict reliably when Latvia's economy will begin to grow again.

Management is unable to estimate reliably the possible effects on the Group's and the Bank's financial position of any further instability in the economies and financial markets of Latvia and other countries in the region as well as the economic downturn in Latvia. Management believes it is taking all the necessary measures to support sustainable growth of the Group's and the Bank's business in the present circumstances

Impact on liquidity:

The volume of wholesale financing has significantly diminished since 2008. Such conditions may affect the Group's and the Bank's ability to obtain new borrowings and to refinance its existing borrowings on terms similar to those applied to earlier transactions. Maturities of the loans repayable by the Group and thew Bank are disclosed in Notes 25 and 40.

NOTES TO THE FINANCIAL STATEMENTS

2 ACCOUNTING POLICIES (continued)

(1) Basis of preparation (continued)

Impact on borrowers:
Borrowers of the Group and the Bank may be affected by the lower liquidity situation which could in turn impact their ability to repay the amounts owed. Deteriorating operating conditions for borrowers may also have an impact on the Management's cash flow forecasts and assessment of the impairment of financial and non-financial assets. The Management based their decisions regarding the recoverable amounts of the assets on the available information, nevertheless it is not possible to predict reliably the impact of the economic downturn.

Impact on collateral:
The amount of provision for impaired loans is based on the Management's appraisals of the assets at the balance sheet date after taking into consideration the cash flows that may result from foreclosure less costs for obtaining and selling the collateral. The market in Latvia for many types of collateral, especially real estate, has been severely affected by the local economic slowdown resulting in there being a low level of liquidity for certain types of assets. As a result, the actual realisable value on foreclosure may differ from the value ascribed in estimating allowances for impairment.

The accompanying financial statements are reported in thousands of lats, unless otherwise stated. Functional currency of the Bank and Group is Latvian lats.

The accounting policies used in the preparation of the financial statements for the period ended 31 December 2009 are consistent with those used in the annual financial statements for the year ended 31 December 2008, except as described in Note 2(26).

(2) Consolidation and investments in subsidiaries

Consolidation
Subsidiary undertakings, in which the Bank, directly or indirectly, has power to exercise control over financial and operating policies, and where operating volumes are substantial, have been consolidated, by adding together similar types of assets, liabilities, income and expenses.

For the purposes of consolidation, all intercompany transactions, balances and unrealised surpluses and deficits on transactions between the Group companies have been eliminated. Where necessary, accounting policies of subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

Subsidiaries
Investments in subsidiaries are accounted for under the cost method in the separate financial statements of the Bank. The Bank recognises income from the investment only to the extent that the Bank receives dividends from the accumulated profits of the subsidiaries arising after the date of acquisition.

Associates
Associates are all entities over which the Group and the Bank has significant influence but not control. Investments in associates are accounted for under cost method in Bank's financial statements and using the equity method in Group's financial statements.

(3) Foreign currency translation

Transactions denominated in foreign currencies are recorded in lats at actual rates of exchange set forth by the Bank of Latvia at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into lats at the rate of exchange prevailing at the end of period. Any gain or loss resulting from a change in rates of exchange subsequent to the date of the transaction is included in the income statement.

NOTES TO THE FINANCIAL STATEMENTS

2 ACCOUNTING POLICIES (continued)

(3) Foreign currency translation (continued)

The applicable rates for the principal currencies held by the Group and the Bank were as follows:

31 December 2009			31 December 2008		
1 EUR	=	LVL 0.702804	1 EUR	=	LVL 0.702804
1 USD	=	LVL 0.489000	1 USD	=	LVL 0.495000
1 GBP	=	LVL 0.783000	1 GBP	=	LVL 0.728000

(4) Income and expense recognition

Interest income and expense are recognised in the income statement for all interest bearing instruments on an accrual basis using the effective interest rate method.

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group estimates cash flows considering all contractual terms of the financial instrument (for example, prepayment options) but does not consider future credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

Fees and commissions are generally recognised on an accrual basis when the service has been provided. Fees related to loans issuing are deferred (together with related direct costs) and recognised as an adjustment to the effective interest rate on the loan.

(5) Trading and investment securities

Trading and investment securities are comprised of the following categories:

- Trading securities comprise fixed income securities and equity shares held by the Bank for trading purposes. They are accounted for at fair value and all gains and losses arising from changes in the fair value are included in the income statement as part of net trading income.
- Investment securities available-for-sale comprise treasury bills and other fixed income securities held by the Bank for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices. They are stated at fair value with all gains and losses from revaluation recognised in the statement of comprehensive income, except for impairment losses, which are recognized in the income statement, until derecognition, at which time the cumulative gain or loss previously recognised in the statement of comprehensive income is recognised in the income statement as part of provision for impairment loss.
- Investment securities held-to-maturity comprise debt securities with fixed or determinable payments and fixed maturities that the Bank's management has the positive intention and ability to hold to maturity. They are carried at amortised cost, that is calculated based on the purchase price of the securities adjusted by discount or premium amortised over the tem of the securities, using the effective interest rate method.

NOTES TO THE FINANCIAL STATEMENTS

2 ACCOUNTING POLICIES (continued)

(5) Trading and investment securities (continued)

The Group assesses at each balance sheet date whether there is objective evidence that available-for-sale and held to maturity investment securities are impaired, either individually or as a class if individually not significant. If any such evidence exists, for available for sale investments the cumulative impairment loss - measured as the difference between the acquisition cost of the asset and the current fair value, less any impairment loss previously recognised - is removed from the statement of comprehensive income and recognised in the income statement. For held to maturity investments the cumulative impairment loss - measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate – is reduced through use of an allowance account and the amount of the loss is recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are not subsequently reversed.

Impairment losses recognised in the income statement on debt instruments are subsequently reversed if a fair value increase is observed that can be objectively related to an event occurring after the impairment loss was recognised. The assessment of the evidence for impairment and the determination of the amount of impairment or its reversal requires the application of management's judgement and estimates.

(6) Due from banks

Amounts due from other banks are recorded when the Group and the Bank advances money to counterparty banks with no intention of trading the resulting unquoted non-derivative receivable due on fixed or determinable dates. Amounts due from other banks are carried at amortised cost.

(7) Loans and receivables

Loans and advances to customers are accounted for as loans and receivables and are carried at amortised cost. Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. All loans are recognised when cash is advanced to borrowers.

For the purposes of these financial statements, finance lease receivables are included in loans and advances to customers.

Management considers risks for all loans to determine the provision for loan impairment and possible losses.

Provisions for individual loan impairment are established if there is objective evidence that it will not be possible to collect all amounts due according to the original contractual terms of loans. The amount of the provision is the difference between the carrying amount and the recoverable amount, being determined as the present value of expected cash flows, including amounts recoverable from guarantees and collateral. Impairment losses are recognised through an allowance account.

In addition to provisions for individual loans, provisions for homogeneous groups of loans based on similarities of credit risk involved, loan size, quality and loan terms are also established. The provision for loan impairment losses for those loans included within homogeneous groups have been estimated based upon historical patterns of losses in each group, the historic pattern of timeliness of payments and reflecting the current economic climate in which the borrowers operate.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account through profit or loss and disclosed as part of provision for impairment loss.

The methodology and assumptions used are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

NOTES TO THE FINANCIAL STATEMENTS

2 ACCOUNTING POLICIES (continued)

(8) Intangible Assets including Goodwill

Acquired computer software and licences are recognised as intangible assets on the basis of the costs incurred to acquire and bring to use the software. These costs are amortised on the basis of their expected useful lives (5 years). Costs associated with developing or maintaining computer software programs are recognised as an expense as incurred.

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net assets of the acquired subsidiary at the date of acquisition. Goodwill on acquisition is reported in the balance sheet as an intangible asset and is measured at cost less any accumulated impairment loss. The goodwill is assessed during each reporting period to determine whether the goodwill is impaired; such impairment loss is determined on the basis of the estimated recoverable amount of the goodwill. The assessment of the impairment of goodwill requires the application of management's judgement, including estimates of future cash flows of the appropriate cash generating unit based on management's business plans, discounted at an appropriate discount rate. Identifiable intangible assets arising on acquisition whose fair value can be measured reliably are recognised separately from goodwill and amortised on a straight-line basis over their expected useful lives. The identification and fair valuation of such intangible assets may require the application of management's judgement and, where applicable, estimates of the attributable cost of the asset or future cash flows from the Group's ownership of the asset discounted at an appropriate discount rate.

(9) Property and equipment

All property and equipment is stated at historical cost less accumulated depreciation. Depreciation is provided using the straight-line method to write off the cost of each asset to its residual value over the estimated useful life of the asset. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.
The annual rates of fixed asset depreciation are:

Category	Depreciation rate
Buildings	2 % p.a.
Furniture and fittings	10 - 20 % p.a.
Computers and equipment	10 - 33 % p.a.
Motor vehicles	17 % p.a.
Leasehold improvements	over the term of the lease agreements

Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. Gains and losses on disposals of property and equipment are recognised in the income statement in the period of disposal. Subsequent costs are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to income statement during the financial period in which they are incurred.. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date. Property and equipment are periodically reviewed for impairment. Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount.

(10) Investment Properties

Investment property comprises land or buildings, which are held in order to earn rentals or for capital appreciation or both, and which are not occupied by the companies in the Group or otherwise held for sale. Property held under operating lease is classified as investment property if, and only if, it meets the definition of an investment property.

Investment property is carried at fair value. Fair value is based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the asset. If this information is not available, the Group uses alternative valuation methods such as discounted cash flow projections. Changes in the fair value of investment property are recorded in the income statement as part of other operating income.

NOTES TO THE FINANCIAL STATEMENTS

2 ACCOUNTING POLICIES (continued)

(11) Leases - when the Group is a lessor

Finance lease receivables at commencement of the lease are recognised at the lower of the fair value of the leased asset or the present value of minimum lease payments. The net investment in finance leases is recorded in the balance sheet net of taxes and the related provision for impairment.

Lease income is recognised over the term of the lease using the net investment method, which reflects a constant periodic rate of return.

Assets under operating leases are recognised as fixed assets at historical cost net of accumulated depreciation. Depreciation is calculated on a straight-line basis to write off the cost of each asset to its residual value over the estimated useful life of fixed assets that is determined based on useful lives of similar assets of the Group.

(12) Financial liabilities carried at amortised cost

Financial liabilities carried at amortised cost are mainly amounts due to customers and due to banks. These are recognised initially at cost, being their issue proceeds (fair value of consideration received) net of transaction costs incurred. Financial liabilities are subsequently stated at amortised cost and any difference between net proceeds and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

(13) Derivative financial instruments

Derivative financial instruments including foreign currency swaps are initially recognised at fair value and subsequently measured at their fair value. Fair values are obtained from quoted market prices and discounted cash flow models as appropriate. All derivatives are carried as assets when fair value is positive and liabilities when the fair value is negative. Changes in the fair value of derivatives are reported in the income statement. The Group and the Bank do not use hedge accounting.

(14) Corporate income tax

Corporate income tax for the reporting period is included in the financial statements based on the management's calculations prepared in accordance with tax legislation of the Republic of Latvia.

Deferred tax is provided in full, using liability method, on all temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. The deferred tax is calculated based on currently enacted tax rates that are expected to apply when the temporary differences reverse. The principal temporary differences arise from different fixed asset depreciation rates, revaluation of investment properties, as well as tax losses carried forward. Deferred tax assets and liabilities are netted only within the individual companies of the Group.

Where an overall deferred taxation asset arises, it is only recognised in the financial statements where it is probable that future taxable profit will be available against which the temporary differences can be utilised.

(15) Cash and cash equivalents

Cash and cash equivalents comprise cash and demand deposits with the Bank of Latvia and other credit institutions, deposits with and from other credit institutions with remaining maturity of 3 months or less.

(16) Mortgage bonds coverage register

The coverage register of mortgage bonds at the Bank is maintained in accordance with the legislation of the Republic of Latvia, including regulatory documents covering mortgage transactions.

NOTES TO THE FINANCIAL STATEMENTS

2 ACCOUNTING POLICIES (continued)

(16) Mortgage bonds coverage register (continued)

The Bank manages mortgage claims included in the coverage register of mortgage bonds according to their remaining value, as well as substitute coverage separately from other assets.

The mortgage claims included in the coverage register of mortgage bonds according to their remaining value are used to ensure that those liabilities that result from the issue of mortgage bonds are met.

Mortgage bonds in circulation according to their total face value are fully covered with mortgage loans. The interest expense on mortgage bonds is covered with the interest income from mortgage loans of the same amount.

(17) Provisions

Provisions are recognised when the Group or the Bank has a present legal or constructive obligation as a result of past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made. These provisions relate to the guarantees issued and other off balance sheet items.

(18) Employee benefits

The Group and the Bank pays social security contributions for state pension insurance and to the state funded pension scheme in accordance with Latvian legislation. State funded pension scheme is a defined contribution plan under which the Group and the Bank pay fixed contributions determined by the law and they will have no legal or constructive obligations to pay further contributions if the state pension insurance system or state funded pension scheme are not able to settle their liabilities to employees. The social security contributions are recognised as an expense on an accrual basis and are included within staff costs.

(19) Fair values of financial assets and liabilities

Fair value is the amount for which assets could be exchanged, or liability settled, between knowledgeable, willing parties in an arms length transaction. Fair values of financial assets or liabilities, including derivative financial instruments, in active markets are based on quoted market prices.

If the market for a financial asset or liability is not active (and for unlisted securities), the Group establishes fair value by using valuation techniques. These include the use of discounted cash flow analysis, option pricing models and recent comparative transactions as appropriate.

Where, in the opinion of the Management, the fair values of financial assets and liabilities differ materially from their book values, such fair values are separately disclosed in the notes to the accounts.

(20) Off-setting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the assets and settle the liability simultaneously.

(21) Recognition and derecognition of financial assets

Purchases and sales of trading securities and investment securities that require delivery within the time frame established by regulation or market convention ("regular way" purchases and sales), are recognised at settlement date, which is the date, when the asset is delivered or given to the Group or the Bank. Any change in the fair value of the asset during the period between the purchase date and the settlement date is recognised in the income statement or in the statement of comprehensive income. Otherwise such transactions are treated as derivative instruments until settlement.

NOTES TO THE FINANCIAL STATEMENTS

2 ACCOUNTING POLICIES (continued)

(21) Recognition and derecognition of financial assets (continued)

The Group and the Bank derecognise financial assets when (a) the assets are redeemed or the rights to cash flows from the assets otherwise expired or (b) the Group and the Bank has transferred the rights to the cash flows from the financial assets or entered into a qualifying pass-through arrangement while (i) also transferring substantially all the risks and rewards of ownership of the assets or (ii) neither transferring nor retaining substantially all risks and rewards of ownership but not retaining control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose additional restrictions on the sale

(22) Initial recognition of financial instruments

Trading securities, derivatives and other financial instruments at fair value through profit or loss are initially recorded at fair value. All other financial instruments are initially recorded at fair value plus transaction costs. Fair value at initial recognition is best evidenced by the transaction price. A gain or loss on initial recognition is only recorded if there is a difference between fair value and transaction price which can be evidenced by other observable current market transactions in the same instrument.

(23) Property held for sale

Property is classified as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. Property held for sale is measured at the lower of its carrying amount and fair value less costs to sell.

(24) Financial guarantees

The Group measures issued financial guarantees initially at their fair value, which is normally evidenced by the amount of fees received. This amount is then amortised on a straight-line basis over the life of the guarantee. At each balance sheet date, the guarantees are measured at the higher of (i) the unamortised balance of the amount at initial recognition and (ii) the best estimate of expenditure required to settle the commitment at balance sheet date.

(25) Off-balance sheet instruments

In the ordinary course of business, the Group and the Bank utilise off-balance sheet financial instruments including commitments to extend loans and advances, financial guarantees and commercial letters of credit. Such financial instruments are recorded in the financial statements when they are funded or related fees are incurred or received. The methodology for provisioning against off-balance sheet instruments is given in Note 2(7*)* above.

(26) Operating segments

Operating segment is different component of Group's activities which is related with offering products and services that are subject to risks and provide revenues that are different from other segments' risks and revenues.

Operating segments with highest revenues received from external customers as well as segments that assets are 10 percent or more of the combined assets of all operating segments are disclosed separately.

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Board of the Bank that makes strategic decisions.

NOTES TO THE FINANCIAL STATEMENTS

2 ACCOUNTING POLICIES (continued)

(27) Critical Accounting Estimates and Judgements

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Such estimates and assumptions are outlined below:

- Impairment losses of loans and advances. The Group reviews its loan portfolio to assess impairment on a regular basis as described in Note 2(7). The Group uses stress tests to determine possible impact of changes in one or more variables used in estimation of the provision for impairment losses on the financial result. To the extent that past due loans in the existing loan portfolio increase by 1%, the provision would be estimated higher by LVL 852 thousand (2008: LVL 653 thousand).
- Impairment on available for sale and held to maturity investments. The Group and the Bank determines that available for sale and held to maturity investments are impaired when the following criteria are met:
    - any instalment is overdue and the late payment cannot be attributed to a delay caused by the settlement systems;
    - the issuer experiences a significant financial difficulty as evidenced by the borrower's financial information that the Group obtains;
    - the issuer considers bankruptcy or a financial reorganisation;
    - there is an adverse change in the payment status of the borrower as a result of changes in the national or local economic conditions that impact the borrower.
- Securities valued at fair value. The Group used quoted market prices to value securities carried at fair value as at year end for those securities which in the management's judgement are traded in active markets. The management had evaluated the activity of the Latvian securities market and has concluded that there is a significant reduction of activities in Latvian market, however, consider the market to be active with respect to type of securities held by the Group therefore quoted market prices available on Riga Stock Exchange were used to determine the fair values of the securities issued by Latvian issuers and traded on Riga Stock Exchange as at year end.

(28) Adoption of new or revised standards and interpretations

Certain new IFRSs became effective for the Group from 1 January 2009. Listed below are those new or amended standards or interpretations which are relevant to the Group's operations and the nature of their impact on the Group's accounting policies.

IAS 1, Presentation of Financial Statements, revised in September 2007. The main change in IAS 1 is the replacement of the income statement by a statement of comprehensive income which includes all non-owner changes in equity, such as the revaluation of available-for-sale financial assets. Alternatively, entities are allowed to present two statements: a separate income statement and a statement of comprehensive income. The Group has elected to present a separate income statement and a statement of comprehensive income. The revised IAS 1 also introduces a requirement to present a statement of financial position (balance sheet) at the beginning of the earliest comparative period whenever the entity restates comparatives due to reclassifications, changes in accounting policies, or corrections of errors. The revised IAS 1 had an impact on the presentation of the Group's financial statements but had no impact on the recognition or measurement of specific transactions and balances.

Improving Disclosures about Financial Instruments - Amendment to IFRS 7, Financial Instruments: Disclosures, issued in March 2009. The amendment requires enhanced disclosures about fair value measurements and liquidity risk. The entity is required to disclose an analysis of financial instruments using a three-level fair value measurement hierarchy. The amendment (a) clarifies that the maturity analysis of liabilities should include issued financial guarantee contracts at the maximum amount of the guarantee in the earliest period in which the guarantee could be called; and (b) requires disclosure of remaining contractual maturities of financial derivatives if the contractual maturities are essential for an understanding of the timing of the cash flows. An entity will further have to disclose a maturity analysis of financial assets it holds for managing liquidity risk, if that information is necessary to enable users of its financial statements to evaluate the nature and extent of liquidity risk. The enhanced disclosures are included in these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

(28) Adoption of new or revised standards and interpretations and new accounting pronouncements (continued)

Improvements to International Financial Reporting Standards (issued in May 2008 endorsed by the EU on 23 January 2009; most of the amendments are effective for annual periods beginning on or after 1 January 2009). The amendments consist of a mixture of substantive changes, clarifications, and changes in terminology in various standards. The substantive changes relate to the following areas: classification as held for sale under IFRS 5 in case of a loss of control over a subsidiary; possibility of presentation of financial instruments held for trading as non-current under IAS 1; accounting for sale of IAS 16 assets which were previously held for rental and classification of the related cash flows under IAS 7 as cash flows from operating activities; clarification of definition of a curtailment under IAS 19; accounting for below market interest rate government loans in accordance with IAS 20; making the definition of borrowing costs in IAS 23 consistent with the effective interest method; clarification of accounting for subsidiaries held for sale under IAS 27 and IFRS 5; reduction in the disclosure requirements relating to associates and joint ventures under IAS 28 and IAS 31; enhancement of disclosures required by IAS 36; clarification of accounting for advertising costs under IAS 38; amending the definition of the fair value through profit or loss category to be consistent with hedge accounting under IAS 39; introduction of accounting for investment properties under construction in accordance with IAS 40; and reduction in restrictions over manner of determining fair value of biological assets under IAS 41. Further amendments made to IAS 8, 10, 18, 20, 29, 34, 40, 41 and to IFRS 7 represent terminology or editorial changes only, which the IASB believes have no or minimal effect on accounting. The amendments did not have a material effect on these financial statements

IFRS 8, Operating Segments. The standard applies to entities whose debt or equity instruments are traded in a public market or that file, or are in the process of filing, their financial statements with a regulatory organisation for the purpose of issuing any class of instruments in a public market. IFRS 8 requires an entity to report financial and descriptive information about its operating segments, with segment information presented on a similar basis to that used for internal reporting purposes. The adoption of IFRS 8 has resulted in the presentation of two main operating standards in the financial statements of the Group – promotional programs and commercial services.

The following new and amended IFRSs and interpretations became effective in 2009, but are not relevant for the Group's operations and did not have an impact on these financial statements.

IAS 23, Borrowing Costs, revised in March 2007.

Puttable Financial Instruments and Obligations Arising on Liquidation—IAS 32 and IAS 1 Amendment.

Vesting Conditions and Cancellations—Amendment to IFRS 2, Share-based Payment.

IFRIC 13, Customer Loyalty Programmes.

IFRIC 14, IAS 19 – The limit on a defined benefit asset, minimum funding requirements and their interaction.

Embedded Derivatives - Amendments to IFRIC 9 and IAS 39.

NOTES TO THE FINANCIAL STATEMENTS

(28) Adoption of new or revised standards and interpretations and new accounting pronouncements (continued)

Certain new standards and interpretations have been published that are mandatory for the Group's accounting periods beginning on or after 1 July 2009 or later periods and which the Group has not early adopted:

IAS 27, Consolidated and Separate Financial Statements (revised January 2008; effective for annual periods beginning on or after 1 July 2009). The revised IAS 27 will require an entity to attribute total comprehensive income to the owners of the parent and to the non-controlling interests (previously "minority interests") even if this results in the non-controlling interests having a deficit balance (the current standard requires the excess losses to be allocated to the owners of the parent in most cases). The revised standard specifies that changes in a parent's ownership interest in a subsidiary that do not result in the loss of control must be accounted for as equity transactions. It also specifies how an entity should measure any gain or loss arising on the loss of control of a subsidiary. At the date when control is lost, any investment retained in the former subsidiary will have to be measured at its fair value. The Group does not expect the amended standard to have a material effect on its financial statements.

IFRS 3, Business Combinations (revised January 2008; effective for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009). The revised IFRS 3 will allow entities to choose to measure non-controlling interests using the existing IFRS 3 method (proportionate share of the acquiree's identifiable net assets) or at fair value. The revised IFRS 3 is more detailed in providing guidance on the application of the purchase method to business combinations. The requirement to measure at fair value every asset and liability at each step in a step acquisition for the purposes of calculating a portion of goodwill has been removed. Instead, in a business combination achieved in stages, the acquirer will have to remeasure its previously held equity interest in the acquiree at its acquisition-date fair value and recognise the resulting gain or loss, if any, in profit or loss for the year. Acquisition-related costs will be accounted for separately from the business combination and therefore recognised as expenses rather than included in goodwill. An acquirer will have to recognise at the acquisition date a liability for any contingent purchase consideration. Changes in the value of that liability after the acquisition date will be recognised in accordance with other applicable IFRSs, as appropriate, rather than by adjusting goodwill. The revised IFRS 3 brings into its scope business combinations involving only mutual entities and business combinations achieved by contract alone. The Group is currently assessing the impact of the amended standard on its financial statements.

Certain new standards and interpretations have been published that become effective for the accounting periods beginning on or after 1 July 2009 or later periods and which are not relevant to the Group or are not yet endorsed by the EU:

Classification of Rights Issues - Amendment to IAS 32 (issued 8 October 2009; effective for annual periods beginning on or after 1 February 2010).

IFRS 1, First-time Adoption of International Financial Reporting Standards (following an amendment in December 2008, effective for the first IFRS financial statements for a period beginning on or after 1 July 2009).

Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate—IFRS 1 and IAS 27 Amendment *(issued in May 2008,* effective from periods beginning on or after 1 July 2009).

Additional Exemptions for First-time Adopters - Amendments to IFRS 1, First-time Adoption of IFRS (effective for annual periods beginning on or after 1 January 2010, *not yet endorsed by the EU*).

Group Cash-settled Share-based Payment Transactions - Amendments to IFRS 2, Share-based Payment (effective for annual periods beginning on or after 1 January 2010, *not yet endorsed by the EU).*

NOTES TO THE FINANCIAL STATEMENTS

(28) Adoption of new or revised standards and interpretations and new accounting pronouncements (continued)

Eligible Hedged Items—Amendment to IAS 39, Financial Instruments: Recognition and Measurement (effective with retrospective application for annual periods beginning on or after 1 July 2009).

Amendment to IAS 24, Related Party Disclosures (effective for annual periods beginning on or after 1 January 2011, *not yet endorsed by the EU*).

IFRS 9, Financial Instruments Part 1: Classification and Measurement.

IFRS 9 adoption is required starting 1 January 2013, yet earlier apply is also allowed, *not yet endorsed by the EU*.

Improvements to International Financial Reporting Standards (issued in April 2009; amendments to IFRS 2, IAS 38, IFRIC 9 and IFRIC 16 are effective for annual periods beginning on or after 1 July 2009; amendments to IFRS 5, IFRS 8, IAS 1, IAS 7, IAS 17, IAS 36 and IAS 39 are effective for annual periods beginning on or after 1 January 2010, *not yet endorsed by the EU).*

IFRIC 12, 'Service concession arrangements' (endorsed by the EU for periods beginning 30 March 2009).

Amendment to IFRIC 14, 'Payments of a minimum funding requirement' (effective for annual periods beginning on or after 1 January 2011, *not yet endorsed by the EU*).

IFRIC 15, Agreements for the Construction of Real Estate (effective 1 January 2009, the EU endorsed from 1 January 2010).

IFRIC 16, Hedges of a Net Investment in a Foreign Operation (effective from 1 July 2009).

IFRIC 17, Distributions of Non-Cash Assets to Owners (effective for annual periods beginning on or after 1 July 2009).

IFRIC 18, Transfers of Assets from Customers (effective for annual periods beginning on or after 1 July 2009, the EU endorsed from annual periods beginning on or after 31 October 2009).

IFRIC 19, Extinguishing financial liabilities with equity instruments (effective for annual periods beginning on or after 1 July 2010*, not yet endorsed by the EU*).

NOTES TO THE FINANCIAL STATEMENTS

3 RISK MANAGEMENT

The Group and the Bank manages all the major risks affecting the operation of the Group and the Bank in accordance with the Risk Management Policy approved by the Council of the Bank. The Risk Management Policy stipulates and describes the aggregate of measures used to ensure that a possibility of suffering losses is minimized in the event the invested or receivable resources would not be repaid or recovered in due time or full amount or the Group or the Bank would suffer other losses or would not derive the planned profit. Risk management is an integral component of the internal control system of the Group and the Bank and the risk management system has been established taking into account the size and structure of the Group and the Bank, as well as the best advisable practice, incl. the guidelines of Basel bank supervisory committee.
In light of the changes occurring on global financial markets and economy, a number of major improvements were made to the risk management system of the Group and the Bank during the reporting period, thus allowing to identify the risks more precisely and timely and to determine their impact on the future operations of the Group and the Bank.

The Group and the Bank abides by the following principles in its risk management:
- while assuming the risks the Group and the Bank shall be capable of implementing the aims and assignments defined in its development strategy in a longer run;
- the Group and the Bank shall operate by maintaining an optimum balance between profitability and safeguarding against the risks, i.e. the profitability must be as large as possible, however, the Group and the Bank shall not be exposed to the risks;
- risk assessment and management shall be an integral component of the every-day functions of the Group and the Bank;
- In accordance with their authority and competence the employees of the Group and the Bank shall know a customer and understand fully the nature of each transaction (operation) to be able to identify and assess the risks associated with the transaction (operation) and find the best solution both for the customer and the Group or the Bank;
- the Group and the Bank shall assess the probable losses that it might incur by assuming the risks and avoid extraordinary losses in its operation;
- the Group and the Bank shall identify and assess the probable risks before launching of new products or services or entering new markets;
- where necessary, the Group and the Bank shall reduce the risk limits, sell the assets subject to the risk or even leave the respective markets should these be assessed as excessively risky.

In managing the risks the Group and the Bank apply various methods and instruments for measuring risks, set the limits and maintain the appropriate controls. All risk policies are approved by the Council.

Credit Risk
The Group and the Bank is subject to the credit risk. The credit risk is the risk of the customer or co-operation partner not being able to or refusing to meet its liabilities towards the Group or the Bank in full amount and due time.
The Group and the Bank manages the credit risk according to the Credit Policy as well as internal regulations, procedures and instructions of credit operations.
The Credit Policy of the Bank describes and defines the principles for the management of the credit risk and it relates to all activities of the Group and the Bank involving credit risk – lending, financial market transactions (operations), intermediary activities on behalf of the clients and issue of guarantees to third parties.
Management process of credit risk within the Group and the Bank encompasses establishment of guidelines and limitations, granting of loans or setting limits to particular clients or groups of interrelated clients; administration, monitoring and evaluation of files of clients or interrelated client groups, as well as appropriate control of the process, operation of management information system and evaluation of the total efficiency of the process.
In establishment of guidelines and limitations, the Group and the Bank primarily follows the common strategy of the Group and the Bank, as well as their historic experience in credit risk management, which allows defining adequate limitations of concentration, as well as adequate assessment of creditworthiness and collateral, passing decisions in decision-making institutions of the appropriate level. As the common strategy of the Group and the Bank encompasses gradual transformation of the Bank into development bank, the risk stemming from implementation of framework funding programmes becomes an increasingly significant risk source for the Group and the Bank.

NOTES TO THE FINANCIAL STATEMENTS

3 RISK MANAGEMENT (continued)

The Bank's Lending department bears the responsibility for daily credit risk management in lending operations, incl. when setting criteria of creditworthiness and collateral adequacy, while decisions about assuming credit risk within the set limits are made by branch, regional and the Central lending committees, or the Board of the Bank. The daily supervision and administration of loans is conducted on the basis of each individual borrower's risk grade and affiliation, determined by organizational structure of the Group and the Bank.

The Risk management committee conducts the integrated monitoring of credit risk, incl. credit risk concentration and loan portfolio quality, while the Risk management department bears the responsibility for analysis of credit risk concentration, setting of limits and their control, quality assessment of the loan portfolio and building of provisions, as well as daily management of credit risk in operations with financial instruments. At least once a year, stress testing of the loan portfolio and scenario analysis is conducted, that includes changes of various macro-environment affecting factors (drop of real estate property prices, households' income decrease, contingent changes in development of various industries of national economy, and similar) and demonstrates the eventual impact on the Group's and the Bank's profitability, loan portfolio quality, volume of provisions and level of capital adequacy.
The Group and the Bank manages credit risk concentrations according to the Risk Exposures Controlling Policy that stipulates the methods of analysis of the credit risk concentrations and its controlling instruments including limits on credit risk concentrations. Credit risk concentration is managed by measuring and setting limits on the following concentrations:

- ratio of large exposure concentration and own funds (internal limit - 400%, limit set by the Law on Credit Institutions – 800%), as of 31.12.2009 was 47.1% (as of 31.12.2008 – 78.6%);
- ratio of single client's (related clients' group) large exposure and own funds, which may not exceed 25%, as of 31.12.2009 was 20.7% (as of 31.12.2008 – 22.1%);
- ratio of risk exposures with persons related to the Bank and own funds, which may not exceed 15%, as of 31.12.2009 was 2.6% (as of 31.12.2008 – 3.8%).
- proportion of risk concentration in a single economic sector in the Bank's credit portfolio and own funds as of 31.12.2009 was 120.9% (as of 31.12.2008 – 172.6%);

Since the Bank's strategy is not focused on servicing the non-residents business, the proportion of the Bank's total claims to non-residents was small and as of 31.12.2009 was 7.1% (as 31.12.2008 – 8.9 %) of the Bank's total assets. The Group and the Bank manages the country risk that results from the lending operations to non-residents according to the Country Risk Management Policy.
Each of the structural units involved in credit risk management maintain an appropriate internal control, efficiency of which is responsibility of the Internal audit department.
The management of the Group and the Bank has performed calculation of losses on the basis of all the facts at its disposal, unbiased proofs of depreciation, and believes the calculations disclosed in the financial reports are reasonable, considering the available information. Nonetheless, having the present awareness, it might occur, as a result of the next year's actual events, differing from the assumptions, that the respective book values of assets and liabilities be corrected.

Liquidity Risk
The liquidity risk relates to the ability of the Group and the Bank to redeem the legally valid claims of its customers and other creditors in due time and secure that the increase of the anticipated claims presents reasonable costs.
The principles for management of liquidity risk are determined by the Liquidity Risk Management Policy and Business Continuity Plan for Liquidity Crisis Situation. The Bank maintains that the liquid assets do not fall below 30% (set by the FCMC) of its short-term liabilities at all times. The Assets and Liabilities Committee of the Bank stipulates the guidelines for liquidity risk management and controls compliance thereof, whereas the Treasury Department provides for daily management of the liquidity risk.
To evaluate the liquidity risk, the Bank uses the GAP method. The Bank has set liquidity net position limit in each significant currency and total liquidity net position limit as well as maximum deposit amount from a single depositor to control the liquidity risk. At least once a month, scenario analysis or stress testing is conducted, to reveal the impact of contingencies on liquidity of the Group and the Bank.
Compliance with the liquidity ratio (min – 30%) was 82.2% as of 31.12.2009 (as of 31.12.2008 – 60.4%).

NOTES TO THE FINANCIAL STATEMENTS

RISK MANAGEMENT (continued)

Liquidity ratio data of the Group and the Bank as of 31 December 2009 are disclosed in Notes 40 to these financial reports.

Foreign Currency Risk

The foreign currency risk occurs due to the differences between the asset and liability positions of foreign currencies that, as a result of the fluctuations of the exchange rates, affect the cash flow and financial results of the Group and the Bank. The principles for the management of the foreign currency risk are outlined in the Currency Risk Management Policy of the Bank.

Monitoring of the foreign currency risk is conducted by the Assets and Liabilities Management Committee of the Bank, whereas the Treasury Department provides for daily management of the foreign currency risk.

The Group and the Bank maintains a cautious foreign currency risk management policy and controls the foreign currency risk by imposing limits on the open currency positions for each currency and all currencies together consolidating in lats and by complying with the open currency position limits established in the law On Credit Institutions. The open currency positions of the Group and the Bank by currency profile as of 31 December 2009 are disclosed in Notes 42 to these financial reports.

Interest Rate Risk

The interest rate risk is related to the influence of the fluctuations of the market rates onto the interest income and expenses of the Group and the Bank. To assess the interest rate risk the Group and the Bank analyses the maturity structure of the assets and liabilities sensitive to the changes in interest rates and susceptibility of the maturity structure to the potential fluctuations of the interest rates on a regular basis. The Assets and Liabilities Management Committee monitors the interest rate risk, whereas the Treasury Department is responsible for the daily management of the interest rate risk. The Bank has set limit on changes in economic value of the Bank at 10% of own funds and limit on changes in net interest income at 2% of own funds which, respectively, were 7.63% as of 31.12.2009 (as of 31.12.2008 – 9.76%) and 0.43% (as of 31.12.2008 – 0.27%). The breakdown of assets and liabilities of the Group and the Bank by profile of time until interest reset date as of 31 December 2009 are disclosed in Notes 41 to these financial reports.

Operational risk

The operational risk results from intentional or unintentional deviations from the standards adopted in daily operation of the Group and the Bank, for example human mistake or fraud, disturbances in the operation of the information systems, insufficient control procedures or their ignorance. The Group and the Bank manages operational risk according to the Operational Risk Management Policy. Self-assessment method is used to measure the operational risk, whereas the Bank's operational risk information system is used to identify, analyse and control the operational risk, which registers and analyses occurrences of operational risk and calculates the scale of actual or potential losses. Structural units of the Group and the Bank are responsible for the management of the operational risk in the daily operations, but the Risk Management Committee supervises the operational risk. The Risk Management Department is responsible for implementation of the operational risk management in the Group and the Bank.

The Bank has implemented Business Continuity Plan that includes guidelines on actions to be taken by the Bank, its structural units and employees at occurrence of risks that can have substantial negative effect on the Bank's operations.

Capital Adequacy

Capital adequacy shows those capital resources of the Group and the Bank needed to cover the credit and market risks arising from asset-side and off-balance sheet positions and also against operational risks.

The Group and the Bank completely follows the requirements of Basel II in their capital adequacy evaluation process. The Group and the Bank uses the standardised approach to calculate minimum capital charge for credit and market risks and basic indicator approach – for operational risk.

As of 31.12.2009, the capital adequacy ratio of the Bank calculated according to the regulations of the Financial and Capital Market Commission were 12.8% (as of 31.12.2008 -9.6%) which exceeded the minimum of 8% for the ratio of the own capital and total of risk-weighted assets and off-balance sheet items.

NOTES TO THE FINANCIAL STATEMENTS

RISK MANAGEMENT (continued)

The expanded calculation of the capital adequacy ratio of the Group and the Bank is provided in Notes 43 to these financial reports.
The Group and the Bank also conducts the internal capital adequacy evaluation process (ICAAP), calculating capital requirements for those significant risks which do not have minimum regulatory capital requirements determined. The results of the internal capital adequacy evaluation as of 31.12.2009 were as follows:

	31/12/09	
	Group	**Bank**
Capital base for internal capital adequacy evaluation	102,733	103,084
Total internal capital requirement	80,745	81,540
Internal capital adequacy ratio	10.2%	10.1%
Surplus of capital base	21,989	21,545

4 REPORT ON CORPORATE GOVERNANCE

The corporate governance of Mortgage Bank is based on the international standards, the best corporate governance practice and laws of the Republic of Latvia.

The daily routine of the Mortgage Bank complies with high standards of corporative governance. The Mortgage Bank constantly works on the improvement of its corporate governance.

The purpose of the corporate governance is to establish, maintain and continuously develop the operational systems that ensure meeting of the targets that the government of the Republic of Latvia has set for the Mortgage Bank, control over operations and management of the operational risks while taking care of customer satisfaction and sustaining good co-operation with the business partners.

Within the framework of corporate governance the Mortgage Bank implements:

- protection of the rights and securing of the interests of the investors, customers and other related parties;
- timely and adequate provision of information about the operations and financial performance and other important events of the Mortgage Bank;
- compliance with generally adopted code of ethics;
- protection of the rights and securing of the interests of the shareholder.

The Mortgage Bank has elaborated and implemented an effective internal control system over the operations of the Bank incorporating the management system of the operational risks of the Bank. The Council and Board of the Bank examine the efficiency of the internal control system on a regular basis, supervise and ensure its constant improvement in line with the changes in the operations of the Mortgage Bank and internal and external circumstances affecting the operations of the Bank.

The internal control system identifies and defines responsibility for maintaining efficient functioning of the specific components of the internal control system by listing the duties and obligations of the shareholder, Council, Board, special committees established by Board, structural units and employees.

In view of the importance of such a component of corporate governance as independent evaluation and control of the financial standing of the Bank, the Council and Board of the Bank guarantee that regarding the drawing up of the financial reports the internal control system gives a true and accurate representation of the operations and financial standing of the Bank.

Within the framework of the internal control system the control processes have been elaborated and documented. The control processes comprise: control over daily operations, supervision and control of drafting of the financial reports and information to be included therein, including independent supervision and control by internal audit, audit committee, external audit and other control institutions.

NOTES TO THE FINANCIAL STATEMENTS

4 REPORT ON CORPORATE GOVERNANCE (continued)

The Mortgage Bank is fully owned by the state of Latvia. The Bank is supervised by the Ministry of Finance of the Republic of Latvia that represents the interests of the shareholder on behalf of the Cabinet of Ministers of the Republic of Latvia and holds 100% of the shares of the Bank.

The Articles of Association of the state-owned JSC "Mortgage and Land Bank of Latvia" govern the election of the Board members and changes to the composition of the Board and mandate of the Board members. The Articles of Association are published on the homepage of the Mortgage Bank. The procedure for making changes to the Articles of Association is governed by the laws of the Republic of Latvia. Once the changes to the Articles of Association are made they are published on the home page of the Bank.

NOTES TO THE FINANCIAL STATEMENTS

5 INTEREST INCOME

	2009		2008	
	Group	**Bank**	**Group**	**Bank**
Interest income:				
- interest on balances due from credit institutions	3,388	3,388	6,334	6,327
- interest on loans to customers	43,941	41,979	55,064	52,517
- interest on investments in securities	7,644	7,629	4,708	4,702
	54,973	**52,996**	**66,106**	**63,546**
Cash flow from interest received	54,902	52,963	64,147	61,573

6 INTEREST EXPENSE

	2009		2008	
	Group	**Bank**	**Group**	**Bank**
Interest expense:				
- interest on balances due to credit institutions	12,729	12,270	27,506	26,632
- interest on current and deposit accounts	13,839	13,843	12,781	12,784
- interest on transit funds	80	80	153	153
- interest on subordinated liabilities	1,803	1,803	1,637	1,637
- interest on mortgage bonds issued	1,950	1,999	2,805	2,805
- other interest expense	49	46	53	53
	30,450	**30,041**	**44,935**	**44,064**
Cash flow from interest paid	34,078	33,343	42,008	41,333

7 FEE AND COMMISSION INCOME

	2009		2008	
	Group	**Bank**	**Group**	**Bank**
Fee and commission income:				
- from lending activities	1,597	1,552	1,325	1,259
- from money transfers and account servicing	1,402	1,406	1,554	1,558
- from payment cards	811	811	982	982
- from securities accounts	272	52	66	66
- from insurance fiduciary activities	133	75	87	87
- other fee and commission income	35	19	77	54
	4,250	**3,915**	**4,091**	**4,006**

8 FEE AND COMMISSION EXPENSE

	2009		2008	
	Group	**Bank**	**Group**	**Bank**
Fee and commission expense:				
- for account services	192	191	213	200
- for payment cards	518	518	604	604
- for transactions with securities	107	295	89	87
- other fee and commission expense	179	21	91	81
	996	**1,025**	**997**	**972**

NOTES TO THE FINANCIAL STATEMENTS

9 NET TRADING INCOME

	2009		2008	
	Group	**Bank**	**Group**	**Bank**
Profit from trading securities	395	372	250	226
Profit / (loss) from securities available for sale	(47)	(47)	-	34
Loss from securities held to maturity	(1,027)	(1,027)	-	-
Profit from dealing with currency exchange and revaluation of foreign currency positions	6,845	7,021	1,906	1,924
	6,166	**6,319**	**2,156**	**2,184**

10 OTHER OPERATING INCOME

	2009		2008	
	Group	**Bank**	**Group**	**Bank**
Income from property privatisation services	270	270	329	329
Penalty fees received on overdue loan repayments	3,017	2,461	1,285	816
Compensations	336	336	761	761
Operating lease income	235	-	231	-
Recovery of loans written off in the previous periods	1,502	1,486	961	961
Other income	1,234	504	1,200	573
	6,594	**5,057**	**4,767**	**3,440**

11 STAFF COSTS

	2009		2008	
	Group	**Bank**	**Group**	**Bank**
Remuneration to the Council and the Board	447	308	613	445
Remuneration to staff members	7,333	6,624	7,686	6,957
Social security contributions	1,845	1,641	1,799	1,593
	9,625	**8,573**	**10,098**	**8,995**

During the reporting year the Bank employed on average 648 staff members (2008: 667).

12 ADMINISTRATIVE AND OTHER OPERATING EXPENSES

	2009		2008	
	Group	**Bank**	**Group**	**Bank**
Training and other staff expense	357	343	593	554
Equipment and premises maintenance expense	2,555	2,373	2,693	2,500
Information system and communication expense	1,614	1,532	1,819	1,716
Advertising and public relations	1,061	841	1,462	1,299
Professional services	675	644	436	431
Property tax	60	60	58	58
Write off of fixed assets	101	101	55	34
Payments to the deposit guarantee fund	510	510	452	452
Revaluation of investment properties	660	660	290	290
Other expenses	1,029	640	1,293	780
	8,622	**7,704**	**9,151**	**8,114**

NOTES TO THE FINANCIAL STATEMENTS

13 PROVISION FOR IMPAIRMENT LOSSES

	2009		2008	
	Group	**Bank**	**Group**	**Bank**
Provision expense:				
- provisions for loans	76,537	76,324	7,886	7,331
- provisions for other assets	2,121	323	360	180
- provisions for securities	2,178	2,178	1,885	1,885
- provisions for investments in subsidiaries	-	235	-	-
- provisions for off balance sheet liabilities	174	174	30	30
	81,010	**79,234**	**10,161**	**9,426**
Release of provision:				
- provisions for loans	(4,557)	(4,551)	(838)	(838)
- provisions for other assets	(491)	(105)	(43)	(43)
- provisions for securities	(344)	(344)	-	-
- provisions for off balance sheet liabilities	(15)	(15)	-	-
	(5,407)	**(5,015)**	**(881)**	**(881)**
Total provision for impairment losses - expense	**75,603**	**74,219**	**9,280**	**8,545**

14 CORPORATE INCOME TAX

	2009		2008	
	Group	**Bank**	**Group**	**Bank**
Income tax	45	-	111	-
Deferred tax	(979)	(1,006)	43	70
Total corporate income tax (income) / expense	**(934)**	**(1,006)**	**154**	**70**

Corporate income tax differs from the theoretically calculated tax amount that would arise applying the 15% rate stipulated by the law to the Bank's and the Group's(loss) / profit before taxation:

	2009		2008	
	Group	**Bank**	**Group**	**Bank**
(Loss) / profit before tax	**(55,344)**	**(55,057)**	**335**	**1,277**
Theoretically calculated tax at a tax rate of 15%	(8,302)	(8,259)	50	192
Dividends received	(1)	(8)	-	(122)
Net income / expenses non deductable for tax purposes	(1,821)	(1,923)	104	-
Change in unrecognized deferred tax asset	9,190	9,184	-	-
Tax (income) / expense for the year ended 31 December	**(934)**	**(1,006)**	**154**	**70**

As at 31 December 2009 the Bank had accumulated tax losses of LVL 66,022, which it can carry forward and utilise in future years. In accordance with the legislation of the Republic of Latvia tax losses carried forward can be covered in chronological order from taxable income during the following eight years.

NOTES TO THE FINANCIAL STATEMENTS

15 CASH AND BALANCES WITH CENTRAL BANK

	31/12/09		31/12/08	
	Group	**Bank**	**Group**	**Bank**
Cash	7,715	7,715	9,184	9,184
Balances with the Bank of Latvia	88,282	88,282	35,931	35,931
	95,997	**95,997**	**45,115**	**45,115**

Balances with the Bank of Latvia reflect the balance of the Bank's correspondent account, on which interest is paid in the amount of the compulsory reserve requirement.

The Bank is required to comply with minimum reserve requirements set by the Bank of Latvia. This requires the Bank's monthly average LVL balance on its correspondent account with the Bank of Latvia to exceed a specified minimum during the maintenance period of requirements.

The Bank was in compliance with the reserve requirement during the reporting period.

16 TRADING AND INVESTMENT SECURITIES

	31/12/09		31/12/08	
	Group	**Bank**	**Group**	**Bank**
Trading securities				
Latvian Treasury bills and government bonds	3,004	3,004	2,150	2,150
Non-OECD government bonds	160	160	-	-
Latvian corporate bonds	1,452	1,452	1,112	1,112
OECD corporate bonds	217	217	344	344
Non-OECD corporate bonds	26	26	46	46
Equity shares in Latvian corporate entities	41	41	41	41
Equity shares in OECD corporate entities	-	-	18	15
Equity shares in non-OECD corporate entities	19	19	-	-
Other investment	155	-	148	3
Total trading securities	**5,074**	**4,919**	**3,859**	**3,711**
Securities held to maturity				
Latvian Treasury bills and government bonds	-	-	101	-
OECD government bonds	1,251	1,251	1,263	1,263
Non-OECD government bonds	7,432	7,432	9,158	9,158
OECD corporate bonds	19,926	19,926	24,522	24,522
Non-OECD corporate bonds	5,889	5,889	14,718	14,718
Latvian corporate bonds	12,111	12,111	16,164	16,164
Total securities held to maturity	**46,609**	**46,609**	**65,926**	**65,825**
Provisions for impairment losses on securities	(3,625)	(3,625)	(1,856)	(1,856)
Total net securities held to maturity	**42,984**	**42,984**	**64,070**	**63,969**
Securities available-for-sale				
Latvian Treasury bills and government bonds	49,892	49,892	26,296	26,296
Total securities available-for-sale	**49,892**	**49,892**	**26,296**	**26,296**
Total net trading and investment securities	**97,950**	**97,795**	**94,225**	**93,976**

NOTES TO THE FINANCIAL STATEMENTS

16 TRADING AND INVESTMENT SECURITIES (continued)

The following table shows the division of the Bank's debt securities by rating agency designation (*Moody`s investors Service*) as at 31 December 2009:

	Trading securities	Investment securities available-for-sale	Securities held to maturity	Total net
Aa1 - Aa3	1,317	-	7,326	8,643
A1 - A3	15	-	5,162	5,177
Baa1 - Baa3	3,164	49,892	13,459	66,515
Lover than Baa3	164	-	8,944	9,108
Unrated	199	-	8,093	8,292
Total	**4,859**	**49,892**	**42,984**	**97,735**

The following table shows the division of the Bank's debt securities by rating agency designation (*Moody`s Investors Service*) as at 31 December 2008:

	Trading securities	Investment securities available-for-sale	Securities held to maturity	Total net
Aaa	-	-	486	**486**
Aa1 - Aa3	293	-	10,345	**10,638**
A1 - A3	-	-	11,039	**11,039**
Baa1 - Baa3	2,150	26,296	12,736	**41,182**
Lover than Baa3	329	-	21,942	**22,271**
Unrated	880	-	7,421	**8,301**
Total	**3,652**	**26,296**	**63,969**	**93,917**

All securities are quoted on stock exchange. The average yield on investment securities as at 31 December 2009 was 6.6% (2008: 7.9%).

17 INVESTMENT PROPERTIES

	31/12/2009		31/12/2008	
	Group	Bank	Group	Bank
Carrying amount at 1 January	**1,826**	**1,826**	**2,116**	**2,116**
Loss on fair valuation	(660)	(660)	(290)	(290)
Carrying amount at 31 December	**1,166**	**1,166**	**1,826**	**1,826**

Investment properties include real estate at Jēkaba iela 6/8, Riga, with a carrying amount of LVL 1,166 thousand as at 31 December 2009 (LVL 1,826 thousand as at 31 December 2008). Investment properties are held at fair value based on valuations made by independent valuers who have up-to-date experience in valuing real estate in the respective location and category and who hold an appropriate professional qualification for real estate valuation. The valuations are made on the basis of recent comparative data in the local market and/or on the basis of rental returns discounted at an appropriate rate.

NOTES TO THE FINANCIAL STATEMENTS

18 DUE FROM CREDIT INSTITUTIONS

	31/12/09		31/12/08	
	Group	**Bank**	**Group**	**Bank**
Due from credit institutions registered in OECD countries	8,923	8,923	5,487	5,487
Due from credit institutions registered in Latvia	25,296	25,161	48,100	47,847
Due from credit institutions registered in other countries	1,192	1,192	12,000	12,000
	35,411	**35,276**	**65,587**	**65,334**

When lending to monetary financial institutions and setting limits for money market and transactions and nostro accounts, the Bank carries out analysis of external credit ratings assigned to correspondent banks and credit institutions as well as assesses their financial and operating performance. During the cooperation period the Bank monitors the performance of correspondent banks and monetary financial institutions and follows up on appropriateness of the limits set in the light of the credit risk assessment. In order to ensure efficient and constructive monitoring of counterparties, the Bank assigns a rating to each counterparty from A (highest) to D (lowest): A – financial performance of the counterparty is stable and the paying capacity is assessed as good in the economic conditions, B – the financial performance of the counterparty is weakening or can lead to potentially serious financial problems in the future, C – the counterparty has serious financial problems that threaten its stability and paying capacity in accordance with the Bank's assessment, D – the counterparty in insolvent or bankrupt in accordance with the information available to the Bank.

The balances due to banks by credit quality of the Bank as at 31 December 2009 is as follows:

	A	**B**	**C**	**D**	**Total**
Due from credit institutions registered in OECD countries	4,363	4,560	-	-	**8,923**
Due from credit institutions registered in Latvia	7,460	5,067	12,634	-	**25,161**
Due from credit institutions registered in other countries	8	53	1,131	-	**1,192**
Total	**11,831**	**9,680**	**13,765**	**-**	**35,276**

The balances due to banks by credit quality of the Bank as at 31 December 2008 is as follows:

	A	**B**	**C**	**D**	**Total**
Due from credit institutions registered in OECD countries	5,296	191	-	-	**5,487**
Due from credit institutions registered in Latvia	27,099	8,844	11,904	-	**47,847**
Due from credit institutions registered in other countries	10,492	1,008	500	-	**12,000**
Total	**42,887**	**10,043**	**12,404**	**-**	**65,334**

At 31 December 2008 the Bank had correspondent accounts with 21 banks (2008: 18 banks).

The average interest rate on balances due from credit institutions as at 31 December 2009 was 0.9% (2008: 4.5%).

NOTES TO THE FINANCIAL STATEMENTS

19 DERIVATIVE FINANCIAL INSTRUMENTS

The Group and the Bank use the following derivative financial instruments: currency forwards representing commitments to purchase foreign and domestic currency, currency swaps representing commitments to exchange one set of cash flows for another. Swaps result in an economic exchange of currencies.

The Group's and the Bank's credit risk represents the potential cost to replace the forward or swap contracts if counterparties fail to perform their obligation. To control the level of credit risk taken, the Group and the Bank assesses counterparties using the same techniques as for its lending activities.

The notional amounts of certain types of financial instruments provide a basis for comparison with instruments recognised on the balance sheet but do not necessarily indicate the amounts of future cash flows involved or the current fair value of the instruments and do not indicate the Group's and the Bank's exposure to credit risks. The derivative instruments become favourable or unfavourable as a result of fluctuations in foreign exchange rates relative to their terms.

The Group's notional amounts and fair values of derivative instruments held for trading are set out in the following table:

	31/12/09			31/12/08		
	Contract / notional amount	Fair value		Contract / notional amount	Fair value	
		Assets	Liabilities		Assets	Liabilities
Currency swaps	86,042	1,950	68	114,828	1,569	522
Currency forwards	3,547	4	87	1,456	12	24
Total		**1,954**	**155**		**1,581**	**546**

20 LOANS TO CUSTOMERS

Loans by type of borrower:

	31/12/09		31/12/08	
	Group	Bank	Group	Bank
Local government	1,614	1,319	1,896	1,530
State owned companies	2,420	2,420	2,934	2,934
Financial institutions	621	70,304	485	77,145
Private companies	483,804	429,800	511,718	431,919
Individuals	205,104	196,841	222,586	211,168
Management / staff	7,468	6,167	7,919	6,216
Public and religious institutions	673	673	690	674
Total gross loans	**701,704**	**707,524**	**748,228**	**731,586**
Accrued interest on loans	5,412	5,418	4,418	4,462
Provisions for impairment losses on loans	(74,435)	(73,441)	(10,260)	(9,473)
Total net loans	**632,681**	**639,501**	**742,386**	**726,575**

97.8% from loans issued by the Bank and the Group are loans to residents of Latvia.

NOTES TO THE FINANCIAL STATEMENTS

20 LOANS TO CUSTOMERS (continued)

Economic sector risk concentrations within the customer loan portfolio are as follows:

	31/12/09		31/12/08	
	Group	**Bank**	**Group**	**Bank**
Agriculture and forestry	90,692	75,857	100,993	85,080
Fishing	3,806	3,730	4,545	4,460
Manufacturing	97,082	88,123	95,418	82,529
Electricity, gas and water utilities	9,863	9,652	7,211	7,130
Construction	40,341	38,327	35,580	31,004
Retail trade and wholesale distribution	55,514	49,168	63,859	50,944
Hotels and restaurants	24,985	24,608	25,094	24,613
Transport, warehousing and communications	33,412	15,254	42,355	17,444
Financial intermediaries	669	70,353	851	77,216
Real estate	80,198	82,336	88,076	88,028
Municipal authorities	1,614	1,319	1,896	1,530
Individuals	212,572	203,008	230,505	217,384
Other industries	50,956	45,789	51,845	44,224
Total gross loans	**701,704**	**707,524**	**748,228**	**731,586**

The extent of loan and advance concentration with respect to individual non-bank customers with total credit exposures equal to or exceeding Ls 1,000 thousand is presented below:

	31/12/09		31/12/08	
	Group	**Bank**	**Group**	**Bank**
Number of customers	73	75	74	76
Total credit exposure of customers	197,327	269,010	184,029	260,659
Percentage of total gross portfolio of loans	28.1%	38.0%	24.6%	35.6%

At 31 December 2009 the top ten borrowers represented 10.3% (9.3% at 31 December 2008) of the total loan portfolio.

The Latvian banking legislation requires that any credit exposure to a non-related entity or group of non-related entities may not exceed 25% of a credit institution's equity and the total credit exposure to all related parties may not exceed 15% of equity. The Latvian Financial and Capital Market Commission has agreed that these limits are not applicable to the Bank's credit exposure to its fully owned leasing subsidiary SIA "Hipolīzings".

As at 31 December 2009, the Bank was in compliance with the legal requirement set for the total amount of non-zero risk credit exposure.

Analysis of loans issued by the Group and the Bank by type of valuation:

	31/12/09		31/12/08	
	Group	**Bank**	**Group**	**Bank**
Individually assessed loans	423,782	430,602	343,718	423,347
Loans assessed on a group basis	208,899	208,899	398,668	303,228
Total net loans	**632,681**	**639,501**	**742,386**	**726,575**

NOTES TO THE FINANCIAL STATEMENTS

20 LOANS TO CUSTOMERS (continued)

The following table provides the division of loans and advances to customers by quality (Bank):

	31/12/09 Bank			31/12/08 Bank		
	Individuals	Companies	Total loans	Individuals	Companies	Total loans
Neither past due nor impaired	125,815	327,405	453,220	168,452	411,120	579,572
Past due but not impaired	27,707	43,148	70,855	31,879	75,139	107,018
Impaired	51,111	137,756	188,867	18,448	31,010	49,458
Total loans	**204,633**	**508,309**	**712,942**	**218,779**	**517,269**	**736,048**
Provisions for impairment losses on loans	(22,120)	(51,321)	(73,441)	(3,423)	(6,050)	(9,473)
Total net loans	**182,513**	**456,988**	**639,501**	**215,356**	**511,219**	**726,575**

Accrued interest on impaired loans as at 31/12/2009 is LVL 3,648 thousand (LVL 1,372 thousand as at 31 December 2008).
The following table provides the division of loans and advances to customers by quality (Group):

	31/12/09 Group			31/12/08 Group		
	Individuals	Companies	Total loans	Individuals	Companies	Total loans
Neither past due nor impaired	132,982	293,910	426,892	180,149	394,432	574,581
Past due but not impaired	29,311	54,630	83,941	32,878	87,393	120,271
Impaired	51,912	144,371	196,283	18,991	38,803	57,794
Total loans	**214,205**	**492,911**	**707,116**	**232,018**	**520,628**	**752,646**
Provisions for impairment losses on loans	(22,299)	(52,136)	(74,435)	(3,530)	(6,730)	(10,260)
Total net loans	**191,906**	**440,775**	**632,681**	**228,488**	**513,898**	**742,386**

The following table provides fair values of collaterals of loans past due for more than 30 days and with outstanding balances exceeding Ls 300 thousand:

	31/12/09		31/12/08	
	Group	Bank	Group	Bank
Loans past due for more than 30 days and outstanding balances exceeding Ls 300 thousand	85,297	85,297	38,995	38,995
Fair value of collateral	**63,544**	**63,544**	**41,028**	**41,028**

Analysis of movement in provisions for loan impairment losses:

	31/12/09		31/12/08	
	Group	Bank	Group	Bank
As at beginning of the year	10,260	9,473	5,006	4,652
Increase of provisions	76,537	76,324	7,886	7,331
Release from provisions	(4,557)	(4,551)	(838)	(838)
Adjustment (foreign exchange fluctuation)	67	67	2	2
Write-off of loans	(7,872)	(7,872)	(1,796)	(1,674)

NOTES TO THE FINANCIAL STATEMENTS

As at end of the year	**74,435**	**73,441**	**10,260**	**9,473**

20 LOANS TO CUSTOMERS (continued)

Maturity profile (Bank):

	31/12/09 Bank			31/12/08 Bank		
	Individuals	**Companies**	**Total loans**	**Individuals**	**Companies**	**Total loans**
Overdue	10,200	26,036	36,236	2,346	7,408	9,754
Falling due within:						
1 month	1,553	15,723	17,276	2,178	16,665	18,843
1 – 3 months	2,407	26,030	28,437	5,421	21,270	26,691
3 – 6 months	3,042	27,839	30,881	3,856	39,568	43,424
6 –12 months	6,104	57,924	64,028	9,083	55,448	64,531
1 – 5 years	56,364	252,757	309,121	51,934	186,629	238,563
more than 5 years	124,963	102,000	226,963	143,961	190,281	334,242
Total loans	**204,633**	**508,309**	**712,942**	**218,779**	**517,269**	**736,048**
Less provision for loan impairment loss	(22,120)	(51,321)	(73,441)	(3,423)	(6,050)	(9,473)
Total net loans to customers	**182,513**	**456,988**	**639,501**	**215,356**	**511,219**	**726,575**

Maturity profile (Group):

	31/12/09 Group			31/12/08 Group		
	Individuals	**Companies**	**Total loans**	**Individuals**	**Companies**	**Total loans**
Overdue	10,411	27,737	38,148	2,454	8,684	11,138
Falling due within:						
1 month	1,765	17,055	18,820	2,413	17,558	19,971
1 – 3 months	2,836	28,939	31,775	5,931	24,608	30,539
3 – 6 months	3,604	31,920	35,524	4,254	42,599	46,853
6 –12 months	7,321	67,135	74,456	10,748	65,146	75,894
1 – 5 years	63,121	217,631	280,752	61,516	169,658	231,174
more than 5 years	125,147	102,494	227,641	144,702	192,375	337,077
Total loans	**214,205**	**492,911**	**707,116**	**232,018**	**520,628**	**752,646**
Less provision for loan impairment loss	(22,299)	(52,136)	(74,435)	(3,530)	(6,730)	(10,260)
Total net loans to customers	**191,906**	**440,775**	**632,681**	**228,488**	**513,898**	**742,386**

The following table provides an analysis of loans and advances to customers past due but not impaired:

	31/12/09 Bank			31/12/08 Bank		
	Individuals	**Companies**	**Total loans**	**Individuals**	**Companies**	**Total loans**

NOTES TO THE FINANCIAL STATEMENTS

Past due up to 30 days	19,696	24,249	43,945	18,551	41,846	60,397
Past due 30-60 days	3,659	8,857	12,516	7,478	16,983	24,461
Past due 60-90 days	2,192	3,935	6,127	3,000	12,045	15,045
Past due over 90 days	2,160	6,107	8,267	2,850	4,265	7,115
Total loans	**27,707**	**43,148**	**70,855**	**31,879**	**75,139**	**107,018**

20 LOANS TO CUSTOMERS (continued)

The following table provides the division of loans and advances to customers past due but not impaired:

	31/12/09 Group			31/12/08 Group		
	Individuals	**Companies**	**Total loans**	**Individuals**	**Companies**	**Total loans**
Past due up to 30 days	21,300	35,731	57,031	19,550	54,100	73,650
Past due 30-60 days	3,659	8,857	12,516	7,478	16,983	24,461
Past due 60-90 days	2,192	3,935	6,127	3,000	12,045	15,045
Past due over 90 days	2,160	6,107	8,267	2,850	4,265	7,115
Total loans	**29,311**	**54,630**	**83,941**	**32,878**	**87,393**	**120,271**

The loans to customers include finance lease receivables. As at 31 December 2009 finance lease receivables may be analysed as follows:

	31/12/09 Group	31/12/08 Group
Falling due within:		
1 month	1,493	1,860
1 – 3 months	3,028	4,018
3 – 6 months	4,340	5,893
6 –12 months	8,758	11,937
1 – 5 years	36,097	52,803
more than 5 years	546	2,644
Total	**54,262**	**79,155**

Finance leases by type of leased assets:

	31/12/09 Group	31/12/08 Group
Manufacturing and agricultural equipment	15,448	18,192
Transport vehicles	38,814	60,963
Total	**54,262**	**79,155**

The average interest rate for the loan portfolio as at 31 December 2009 was 5.5% per annum (7.8% at 31 December 2008).

21 INVESTMENTS IN SUBSIDIARIES AND ASSOCIATED UNDERTAKINGS

The Bank's direct investments in subsidiaries and associated entities are specified as follows:

	Share capital	Total equity	Bank's share (%)	Investment value 31/12/09	Investment value 31/12/07

NOTES TO THE FINANCIAL STATEMENTS

SIA "Hipolīzings"	645	564	100%	300	300
SIA "Hipotēku bankas nekustamā īpašuma aģentūra"	915	238	100%	680	50
SIA „Risku investīciju sabiedrība"	500	515	100%	500	500
KS „Mazo un vidējo komersantu atbalsta fonds"	101	90	47.62%	48	48
Total				**1,528**	**898**

21 INVESTMENTS IN SUBSIDIARIES AND ASSOCIATED UNDERTAKINGS (continued)

The consolidation group also includes the following entities: IPS „Hipo Fondi" (83% owned by SIA „Risku investīciju sabiedrība") and SIA „Rīgas centra namu pārvalde" (100% owned by SIA „Risku investīciju sabiedrība").

In the reporting period the equity capital of SIA „Hipotēku bankas nekustamā īpašuma aģentūra" (Real Estate Agency of the Mortgage Bank) was increased by LVL 865 thousand and as at 31 December 2009 amounted to LVL 915 thousand (as at 31 December 2008 – LVL 50 thousand).

For impairment testing purposes Mortgage bank has valued its subsidiary SIA "Hipotēku bankas nekustamā īpašuma aģentūra" as individual cash generating unit. The recoverable amount of the subsidiary, being individual cash generating unit, has been determined based on value in use calculation. The calculation is based on projected cash flows in accordance with the financial plan for 2010 – 2013 and discount rate of 9%, which are the estimated Group weighted average risk and capital costs considering the establishment purpose and tasks of the subsidiary. The financial plan and business volumes for the subsidiary for the next five years are based on the overall economic situation and financial sector in particular. The financial plan is largely rooted in development of the real estate market in the coming years that will directly affect the cash flows and financial data of the subsidiary. Major assumptions are gradual stabilisation of the real estate market, including increase of real estate liquidity, moderate price rise depending on the type of real estate as well as prudent forecast that rental income will cover the maintenance expenses of real estate, such as management, insurance, security services, utility payments.

As at 31 December 2009 the carrying amount of cash generating unit exceeded its estimated value in use. Therefore impairment loss in the amount of LVL 235 thousand was recognised as expense in the reporting period.

22 INTANGIBLE ASSETS

The following is included in the net book value of intangible assets:

	31/12/09		31/12/08	
	Group	**Bank**	**Group**	**Bank**
Computer software	1,800	1,721	2,030	1,942
Goodwill arising on acquisition	404	-	404	-
Total intangible assets	**2,204**	**1,721**	**2,434**	**1,942**

The following table presents movements in the Group's and the Bank's net book value of compute software:

	Group	**Bank**
Historical cost		
As at 1 January 2009	**5,000**	**4,847**
Additions	285	281
As at 31 December 2009	**5,285**	**5,128**

NOTES TO THE FINANCIAL STATEMENTS

Accumulated depreciation		
As at 1 January 2009	**2,970**	**2,905**
Charge for the period	515	502
As at 31 December 2009	**3,485**	**3,407**
Net book value as at 31 December 2008	**2,030**	**1,942**
Net book value as at 31 December 2009	**1,800**	**1,721**

23 PROPERTY AND EQUIPMENT

The following table shows changes in property and equipment of the Bank in 2009:

	Land and buildings	Vehicles	Equipment	Leasehold improvements	Total
Cost					
As at 1 January 2009	**4,111**	**1,016**	**9,654**	**1,408**	**16,189**
Additions	58	53	579	3	693
Disposals	-	(113)	(316)	(70)	(499)
As at 31 December 2009	**4,169**	**956**	**9,917**	**1,341**	**16,383**
Accumulated depreciation					
As at 1 January 2009	**569**	**571**	**6,948**	**463**	**8,551**
Charge for the period	81	137	958	156	1,332
Disposals	-	(102)	(293)	(1)	(396)
As at 31 December 2009	**650**	**606**	**7,613**	**618**	**9,487**
Net book value					
As at 31 December 2009	**3,519**	**350**	**2,304**	**723**	**6,896**

The following table shows changes in property and equipment of the Bank in 2008:

	Land and buildings	Vehicles	Equipment	Leasehold improvements	Total
Cost					
As at 1 January 2008	**4,092**	**1,112**	**8,818**	**1,459**	**15,481**
Additions	19	141	1,031	64	1,255
Disposals	-	(237)	(195)	(115)	(547)
As at 31 December 2008	**4,111**	**1,016**	**9,654**	**1,408**	**16,189**
Accumulated depreciation					
As at 1 January 2008	**489**	**625**	**6,014**	**406**	**7,534**
Charge for the period	80	170	1,123	150	1,523
Disposals	-	(224)	(189)	(93)	(506)
As at 31 December 2008	**569**	**571**	**6,948**	**463**	**8,551**
Net book value					
As at 31 December 2008	**3,542**	**445**	**2,706**	**945**	**7,638**

The following table shows changes in property and equipment of the Group in 2009:

	Land and Buildings	Vehicles	Equipment	Leasehold improvements	Total
Cost					
As at 1 January 2009	**4,226**	**2,007**	**9,950**	**1,474**	**17,657**
Additions	58	176	585	3	822
Disposals	-	(594)	(327)	(111)	(1,032)
As at 31 December 2009	**4,284**	**1,589**	**10,208**	**1,366**	**17,447**
Accumulated depreciation					
As at 1 January 2009	**592**	**792**	**7,088**	**478**	**8,950**

NOTES TO THE FINANCIAL STATEMENTS

Charge for the period	85	273	1,002	161	1,521
Disposals	-	(248)	(303)	(9)	(560)
As at 31 December 2009	**677**	**817**	**7,787**	**630**	**9,911**
Net book value					
As at 31 December 2009	**3,607**	**772**	**2,421**	**736**	**7,536**

NOTES TO THE FINANCIAL STATEMENTS

23 PROPERTY AND EQUIPMENT (continued)

The following table shows changes in property and equipment of the Group in 2008:

	Land and Buildings	Vehicles	Equipment	Leasehold improvements	Total
Cost					
As at 1 January 2008	**4,346**	**1,782**	**9,114**	**1,520**	**16,762**
Additions	19	647	1,092	69	1,827
Disposals	(139)	(422)	(256)	(115)	(932)
As at 31 December 2008	**4,226**	**2,007**	**9,950**	**1,474**	**17,657**
Accumulated depreciation					
As at 1 January 2008	**531**	**713**	**6,131**	**412**	**7,787**
Charge for the period	88	389	1,193	159	1,829
Disposals	(27)	(310)	(236)	(93)	(666)
As at 31 December 2008	**592**	**792**	**7,088**	**478**	**8,950**
Net book value					
As at 31 December 2008	**3,634**	**1,215**	**2,862**	**996**	**8,707**

24 OTHER ASSETS

	31/12/09		31/12/08	
	Group	**Bank**	**Group**	**Bank**
Financial assets	2,548	2,040	1,782	1,500
Non-financial assets	7,001	129	3,455	62
Total other assets (gross)	**9,549**	**2,169**	**5,237**	**1,562**
Impairment provision	(653)	(304)	(237)	(106)
Total other assets (net)	**8,896**	**1,865**	**5,000**	**1,456**

25 DUE TO CREDIT INSTITUTIONS

	31/12/09		31/12/08	
	Group	**Bank**	**Group**	**Bank**
Due to credit institutions registered in OECD area	361,226	361,226	496,249	476,948
Due to credit institutions registered in Latvia	18,286	18,286	18,979	18,979
	379,512	**379,512**	**515,228**	**495,927**

Maturity profile:

	31/12/09		31/12/08	
	Group	**Bank**	**Group**	**Bank**
Falling due within:				
1 month	21,959	21,959	15,607	15,607
1 – 3 months	5,885	5,885	6,883	6,557
3 – 6 months	28,817	28,817	18,807	18,807
6 –12 months	123,535	123,535	138,467	119,392
1 – 5 years	136,676	136,676	290,051	290,051
more than 5 years	62,640	62,640	45,413	45,513
	379,512	**379,512**	**515,228**	**495,927**

NOTES TO THE FINANCIAL STATEMENTS

25 DUE TO CREDIT INSTITUTIONS (continued)

Due to credit institutions include the following syndicated loans which totaled to 184 mln LVL:

Lender/arranger	Amount	Currency	Maturity
Standard Bank Plc (14 participants)	177,500	EUR	30.08.2010.
Sumitomo Mitsui Banking Corporation (3 participants)	18,488	EUR	15.06.2012.
Raiffeisen Zentralbank Osterreich (15 participants)	85,000	EUR	16.06.2012.

These syndicated loans were received between 2004 and 2006, the time when both global and Latvian economic processes were favorable for attraction of such financial resources. There were 5 (five) transactions conduced in total, for the total amount of 497.5 mln EUR with maturities varying from 3 to 7 years. The major part of the fund received was used by the Bank for lending to small and medium enterprises.

According to the Loan Market Association (LMA) standards, syndicated loan agreements contain a number of financial covenants that has to be met by the borrower (the Bank). The most covenants are related to: capital adequacy ratio, net tangible worth, liquidity ratio, non-performing loans and investment grade rating.

Taking to account high probability of systemic support provided by the government of the Republic of Latvia, long term foreign currency deposit rating of the Bank is being directly tied to country rating (country ceiling) and, actually, is beyond the influence of the Bank.

In the reporting period as a result of the global economic downturn and Latvian financial crisis, the Bank breached certain of its debt covenants relating to loans due to credit institutions because of the ratio of non-performing loans to the total loan portfolio. The Bank negotiated with the lenders the waivers to the covenants. At the end of the reporting period the negotiations produced consent on the major terms of the changes to the agreements. The official changes to the agreements with the syndicated lenders have been made at the end of 2009 – beginning of 2010.

The maturity profile above and the maturity analysis in Note 40 classifies the related borrowings with their current contractual maturities.

The management of the Bank has conducted situation modelling and liquidity assessment assuming that syndicated loans from the lenders who had not yet made the formal changes to the agreements as at 31 December 2009 and which as at 31 December 2009 amount to 70,133 thousand LVL, are classified as liabilities on demand. The Bank's liquidity ratio, with this assumption, would drop from 82.2% to 62.6%. The liquidity ratio assessed in both cases considerably exceeds the regulator's (the FCMC) requirement of 30%.

The average interest rate for due to credit institutions as at 31 December 2009 was 2.4% (at 31 December 2008: 4.7%).

26 DUE TO CUSTOMERS

	31/12/09		31/12/08	
	Group	Bank	Group	Bank
Central government	962	962	5,000	5,000
Local government	3,411	3,411	5,166	5,166
State owned companies	8,034	8,034	4,499	4,499
Financial institutions	55,298	55,336	32,559	32,639
Private companies	41,769	41,793	43,844	43,875
Individuals	206,742	206,742	202,125	202,125
Public and religious organisations	4,996	4,996	5,196	5,196
	321,212	**321,274**	**298,389**	**298,500**
Accrued interest	3,537	3,537	3,709	3,709
Total due to customers	**324,749**	**324,811**	**302,098**	**302,209**

NOTES TO THE FINANCIAL STATEMENTS

26 DUE TO CUSTOMERS (continued)

Due to customers analysis by term:

	31/12/09		31/12/08	
	Group	**Bank**	**Group**	**Bank**
On demand	63,179	63,214	67,880	67,991
Term balances	261,570	261,597	234,218	234,218
Total due to customers	**324,749**	**324,811**	**302,098**	**302,209**

98.9% of the deposits with the Bank are the Bank's liabilities to residents of Latvia, the remaining 1.1% of the deposits are liabilities to other countries residents.

The average interest rate for demand deposits at 31 December 2009 was 0.4% (0.4% at 31 December 2008), for term deposits – 5.9% (6.5% at 31 December 2008).

27 ISSUED DEBT SECURITIES

	31/12/09	31/12/08
	Bank	**Bank**
Mortgage bonds	38,249	40,660
Total	**38,249**	**40,660**

The purpose of mortgage bonds issuing was to attract financial resources for refinancing of the long-term mortgage loans. The purpose of debt securities issuing was to attract financial resources for financing general Bank activities.

All mortgage bonds issued by the Bank are assigned Baa2 rating by Moody's Investors Service. All issued debt securities are quoted on the Official List of the Riga Stock Exchange.

The average annual interest rate of the issued securities was 4.9% (as at 31 December 2008: 5.8%).

Statement on Mortgage bond coverage as at 31 December 2009

(a) Issued mortgage bonds

ISIN	Security class	Number of mortgage bonds	Face value	Registered volume, currency	Coupon rate, %	Maturity date	Outstanding volume, LVL	Book value, LVL
LV0000800266	AN	30,000	100 LVL	3,000,000	17.5%*	15.08.2010.	3,000,000	3,179,168
LV0000800100	AH	20,000	100 LVL	2,000,000	7.5%	15.08.2011.	1,129,300	1,181,395
LV0000800217	BA	100,000	100 USD	10,000,000	1.625%**	15.08.2011.	2,934,000	2,952,012
LV0000800688	C01CC	250,000	100 EUR	25,000,000	5.70%	15.02.2011.	8,953,020	9,111,480
LV0000800340	CA	200,000	100 EUR	20,000,000	1.4375***	15.02.2012.	13,643,112	13,717,202
LV0000800142	AL	50,000	100 LVL	5,000,000	6.0%	15.08.2012.	4,377,600	4,472,909
LV0000800159	AM	70,000	100 LVL	7,000,000	5.25%	15.08.2013.	3,573,800	3,634,401
						Total	**37,610,832**	**38,248,567**

* floating coupon rate (6 month RIGIBOR plus 0.5%) that is revised twice every year on 15 February and 15 August
** floating coupon rate (6 month LIBOR plus 0.8%) that is revised twice every year on 15 February and 15 August
***floating coupon rate (6 month EURIBOR plus 0.29%) that is revised twice every year on 15 February and 15 August

NOTES TO THE FINANCIAL STATEMENTS

27 ISSUED DEBT SECURITIES (continued)

(b) Structure of Mortgage bond coverage

Mortgage bonds in circulation are secured by assets included in the Mortgage Bond Cover Register which as of 31 December 2009 amounted to LVL 94,666 thousand (as at 31 December 2008: LVL 120,219 thousand). Assets included in the Mortgage Bond Cover Register consisted of mortgage loans (ordinary cover) in the amount of LVL 85,186 thousand (as at 31 December 2008: LVL 114,317 thousand) and substitute cover amounting to LVL 9,480 thousand (as at 31 December 2008: LVL 5,902 thousand).

As at 31 December 2009, the amount of assets included in the Mortgage Bond Cover Register exceeds the amount of mortgage bonds in circulation by 65.4% (as at 31 December 2008: 68.4%) of the amount of weighted assets included in the Mortgage Bond Cover Register (minimum statutory requirement: 10%).

(c) Analysis of mortgage loans included in Mortgage bond coverage by type of real estate

	31/12/09 Bank	31/12/08 Bank
Residential mortgage loans	54,647	69,851
Commercial mortgage loans	30,539	44,466
Total	**85,186**	**114,317**

28 DEFERRED TAX LIABILITIES

Movements in the provision for deferred tax liability:

	31/12/09		31/12/08	
	Group	Bank	Group	Bank
Deferred tax liability at the beginning of the reporting year	**1,006**	**1,006**	**963**	**936**
Change in deferred tax liabilities	(979)	(1,006)	43	70
Deferred tax liability at the end of the reporting year	**27**	**-**	**1,006**	**1,006**

Deferred income tax assets and liabilities are attributable to the following items:

	31/12/09		31/12/08	
	Group	Bank	Group	Bank
Deferred tax liabilities:	**917**	**825**	**1,175**	**1,075**
Temporary difference of property and equipment depreciation	798	706	918	818
Revaluation of investment property	119	119	218	218
Other temporary differences	-	-	39	39
Deferred tax assets:	**10,080**	**10,009**	**169**	**69**
Provision for employee holiday pay	80	71	70	63
Other temporary differences	35	35	99	6
Tax loss carried forward*	9,965	9,903	-	-
Total deferred tax liability	**27**	**-**	**1,006**	**1,006**
Unrecognized deferred tax asset*	**(9,190)**	**(9,184)**	**-**	**-**

* Deferred tax asset was not recognized according to the policy (14) described in the Note 2 *Accounting*

NOTES TO THE FINANCIAL STATEMENTS

policies.

NOTES TO THE FINANCIAL STATEMENTS

29 OTHER LIABILITIES

	31/12/09		31/12/08	
	Group	**Bank**	**Group**	**Bank**
Financial liabilities				
Support programmes financing*	23,777	23,777	9,249	9,249
Other financial liabilities	3,623	3,058	3,834	3,130
	27,400	**26,835**	**13,083**	**12,379**

* Co-financing for realisation of European Social Fund programme "Training, consulting and financial support for commercial activity and self-employment undertakers" and European Regional Development Fund programme "Lending for undertakers of commercial activity".

30 SUBORDINATED LIABILITIES

On 27 November 2003, an agreement was concluded between the Bank and the State Treasury on issuing of a subordinated debt of LVL 10,000 thousand, with a maturity of 7 February 2013 and an interest rate of 5.6 % as at 31 December 2009.

On 31 March 2008, an agreement was concluded between the Bank and the State Treasury on issuing of a subordinated debt of EUR 30,000 thousand, with a maturity of 30 April 2015 and an interest rate of 5.78 % as at 31 December 2009.

31 SHARE CAPITAL

Share capital as at 31 December 2009 and 31 December 2008 was as follows:

		31/12/09		31/12/08
Fully paid share capital	**Number**	**LVL**	**Number**	**LVL**
Ordinary shares	121,320,911	121,320,911	48,513,143	48,513,143
Total fully paid share capital	**121,320,911**	**121,320,911**	**48,513,143**	**48,513,143**

According to the Articles of Association, the fully paid share capital of the Bank consists of 121,320,911 ordinary shares in the total amount of LVL 121,320,911, owned by the Republic of Latvia. The nominal value of each share is LVL 1.

On the basis of the Cabinet of Ministers decree No 275 dated 22 May 2008 and decree No 607 dated 4 September 2009 the equity capital of the Bank was increased by LVL 29,518 thousand and LVL 43,290 thousand respectively.

In 2009, the Bank distributed LVL 966 thousand to the Ministry of Finance for the use of the state funds from the profit for 2008.

Reserve capital of the Bank consists of undistributed profits from 2003 in the amount of LVL 1,249 thousand, which have been transferred to reserve capital. This part of the reserve is distributable based on shareholder decision. The remaining part of the reserve capital is shareholder contribution in kind and reserves of an acquired company. This part of the reserve capital is non-distributable.

Reserve capital of the Group consists of Reserve capital of the Bank and undistributed profits from previous years of SIA "Hipotēku bankas nekustamā īpašuma aģentūra" in the amount of LVL 549 thousand and is distibutable based on shareholder decision.

NOTES TO THE FINANCIAL STATEMENTS

32 CASH AND CASH EQUIVALENTS

	31/12/09		31/12/08	
	Group	**Bank**	**Group**	**Bank**
Cash	7,715	7,715	9,184	9,184
Placements with the Bank of Latvia	88,282	88,282	35,931	35,931
Placements with other credit institutions	27,035	26,900	23,843	23,620
Placements with other credit institutions with remaining maturity up to 3 months	6,136	6,136	10,988	10,958
Placements from other credit institutions with remaining maturity up to 3 months	(27,844)	(27,844)	(22,490)	(22,164)
	101,324	**101,189**	**57,456**	**57,529**

33 RELATED PARTY TRANSACTIONS

Related parties are defined as shareholder who has significant influence over the Bank, members of the Council, the Board of Directors and the Bank's higher level management, their close relatives and companies in which they have a controlling interest as well as Bank's subsidiaries and companies, in which the Bank is having a significant influence.

The following loans and deposits were held with related parties at 31 December 2009:

	31/12/09	31/12/08
	Bank	**Bank**
Loans:		
- Members of the Council, the Board and high level management	1,260	1,867
- subsidiaries	73,765	78,545
- other related parties	3,261	3,800
Total loans held by related parties	**78,286**	**84,212**
Deposits:		
- Members of the Council and the Board and high level management	479	463
- subsidiaries	63	88
- other related parties	1,067	347
Total deposits held by related parties	**1,609**	**898**

Bank's income / (expenses) from transactions with related parties:

	2009	2008
	Bank	**Bank**
Interest income from loans to related parties	2,775	5,249
Interest expenses for deposits held from related parties	(129)	(35)
Total income, net	**2,646**	**5,214**

The average interest rate as at 31 December 2009 on loans issued to related parties was 2.5% per annum (6.4% as at 31 December 2008). The average interest rate as at 31 December 2009 on deposits held for related parties was 4.6% per annum (3.1% as at 31 December 2008).

NOTES TO THE FINANCIAL STATEMENTS

33 RELATED PARTY TRANSACTIONS (continued)

Table below provides assets and liabilities of the Bank related to transactions with the government of the Republic of Latvia, state controlled entities and institutions:

	31/12/09 Bank	31/12/08 Bank
Assets:		
Latvian Treasury bills and government bonds	52,896	28,446
Loans to state controlled entities	2,420	2,934
Total	**55,316**	**31,380**
Liabilities:		
Subordinated liabilities	31,089	31,089
Deposits of central government and state controlled entities	8,996	9,499
Total	**40,085**	**40,588**

Bank's income / (expenses) from transactions with the government of the Republic of Latvia, state controlled entities and institutions:

	2009 Bank	2008 Bank
Interest income	5,025	1,182
Interest expense	(2,313)	(2,061)
Total expenses, net	**2,712**	**(879)**

34 SEGMENT ANALYSIS

Group's operations are managed based on two operating segments:

Promotional programs: operating segment comprises loans to particular SME's or individuals according to priorities defined by the Government or within the scope of European Union promotional programs.

Commercial services (Bank): operating segment comprises Bank's services to individuals and legal entities, loans to customers, accounts, savings and investments, serving payment cards.

Commercial services (Associated companies): operating segment comprises associated companies' services with real estate, leasing and asset management.

NOTES TO THE FINANCIAL STATEMENTS

34 SEGMENT ANALYSIS (continued)

2009 Group	Promotional programs	Commercial services Bank	Commercial services Associated comp.	Reconciliation	Group
Revenue form external customers	12,406	53,205	6,377	-	71,988
Intersegment revenue	219	9,173	405	(9,797)	-
Total revenues	**12,625**	**62,378**	**6,782**	**(9,797)**	**71,988**
External expense	(31,645)	(91,346)	(4,341)	-	(127,332)
Intersegment expense	(6,492)	(624)	(2,681)	9,797	-
Total expenses	**(38,137)**	**(91,970)**	**(7,022)**	**9,797**	**(127,332)**
Loss before income tax	**(25,512)**	**(29,592)**	**(240)**	**-**	**(55,344)**
Income tax expense	-	-	-	-	- 934
Net loss for the period	**(25,512)**	**(29,592)**	**(240)**	**-**	**- (54,410)**
Dividend from other segments	-	47	-	(47)	-
Total revenue comprise:					
Interest income	11,858	38,968	4,147	-	54,973
Interest income from other segments	219	5,688	52	(5,959)	-
Fee and commission income	234	3,203	813	-	4,250
Fee and commission income from other segments	-	2,826	-	(2,826)	-
Other income	314	11,034	1,417	-	12,765
Other income from segments	-	659	353	(1,012)	-
Total revenue	**12,625**	**62,378**	**6,782**	**(9,797)**	**71,988**
Total expense comprise:					
Interest expense	(2,554)	(27,435)	(461)	-	(30,450)
Interest expense to other segments	(3,518)	(271)	(2,170)	5,959	-
Fee and commission expense	-	(996)	-	-	(996)
Fee and commission expense to other segments	(2,348)	-	(478)	2,826	-
Administrative expenses	(542)	(15,411)	(2,294)	-	(18,247)
Administrative expenses and other operating expenses to other segments	(626)	(353)	(33)	1,012	-
Depreciation and amortization	(24)	(1,810)	(202)	-	(2,036)
Provision for impairment losses	(28,525)	(45,694)	(1,384)	-	(75,603)
Total expense	**(38,137)**	**(91,970)**	**(7,022)**	**9,797**	**(127,332)**
Dividend from other segments	-	47	-	(47)	-

NOTES TO THE FINANCIAL STATEMENTS

34 SEGMENT ANALYSIS (continued)

31/12/09 Group	Promotional programs	Commercial services Bank	Commercial services Associated comp.	Reconciliation	Group
Reportable segment assets	**282,915**	**721,318**	**78,530**	-	-
Segment assets comprise:					
Cash and balances with Central Bank	-	95,997		-	95,997
Securities	-	97,795	155	-	97,950
Securities to other segments	-	-	820	(820)	-
Due from credit institutions	-	35,276	135	-	35,411
Due from other segments	35,843	84,159	62	(120,064)	-
Loans to customers	246,813	317,902	67,966	-	632,681
Loans to other segments	-	74,786	-	(74,786)	-
Other assets	259	13,047	9,392	-	22,698
Other assets to other segments	-	2,356	-	(2,356)	-
Total assets	**282,915**	**721,318**	**78,530**	**(198,026)**	**884,737**
Reportable segment liabilities and shareholder's equity	**282,915**	**721,318**	**78,530**	-	-
Segment liabilities comprise:					
Due to credit institutions	118,496	261,016	-	-	379,512
Due to other segments	51,086	35,843	73,786	(160,715)	-
Due to customers	-	324,749	-	-	324,749
Due to other segments (deposits)	-	62	-	(62)	-
Issued debt securities	-	37,429	-	-	37,429
Issued debt securities to other segments	-	820	-	(820)	-
Other liabilities	26,470	5,846	1,256	-	33,572
Other liabilities to other segments	33,073	-	1,876	(34,949)	-
Subordinated liabilities	-	31,089	-	-	31,089
Shareholders equity	53,790	24,464	132	-	78,386
Shareholders equity to other segments	-	-	1,480	(1,480)	-
Total liabilities and shareholder's equity	**282,915**	**721,318**	**78,530**	**(198,026)**	**884,737**

NOTES TO THE FINANCIAL STATEMENTS

34 SEGMENT ANALYSIS (continued)

2008 Group	Promotional programs	Commercial services Bank	Commercial services Associated comp.	Reconciliation	Group
Revenue from external customers	7,938	60,160	9,035	-	77,133
Intersegment revenue	273	8,429	97	(8,799)	-
Total revenues	**8,211**	**68,589**	**9,132**	**(8,799)**	**77,133**
External expense	(5,071)	(67,544)	(4,183)	-	(76,798)
Intersegment expense	(3,338)	(370)	(5,091)	8,799	-
Total expenses	**(8,409)**	**(67,914)**	**(9,274)**	**8,799**	**(76,798)**
(Loss) / profit before income tax	**(198)**	**675**	**(142)**	**-**	**335**
Income tax expense	-	-	-	-	- (154)
Net profit for the period	(198)	675	(142)	-	181
Dividend from other segments	-	800	-	(800)	-
Total revenue comprise:					
Interest income	6,884	51,598	7,624	-	66,106
Interest income from other segments	273	6,321	3	(6,597)	-
Fee and commission income	235	3,745	111	-	4,091
Fee and commission income from other segments	-	1,628	-	(1,628)	-
Other income	819	4,817	1,300	-	6,936
Other income from segments	-	480	94	(574)	-
Total revenue	**8,211**	**68,589**	**9,132**	**(8,799)**	**77,133**
Total expense comprise:					
Interest expense	(3,568)	(40,493)	(874)	-	(44,935)
Interest expense to other segments	(1,257)	(276)	(5,064)	6,597	-
Fee and commission expense	-	(972)	(25)	-	(997)
Fee and commission expense to other segments	(1,602)	-	(26)	1,628	-
Administrative expenses	(555)	(16,460)	(2,234)	-	(19,249)
Administrative expenses and other operating expenses to other segments	(479)	(94)	(1)	574	-
Depreciation and amortization	(25)	(1,997)	(315)	-	(2,337)
Provision for impairment losses	(923)	(7,622)	(735)	-	(9,280)
Total expense	**(8,409)**	**(67,914)**	**(9,274)**	**8,799**	**(76,798)**
Dividend from other segments	-	800	-	(800)	-

NOTES TO THE FINANCIAL STATEMENTS

34 SEGMENT ANALYSIS (continued)

31/12/08 Group	Promotional programs	Commercial services Bank	Commercial services Associated comp.	Reconciliation	Group
Reportable segment assets	**124,034**	**879,922**	**102,222**	**-**	**-**
Segment assets comprise:					
Cash and balances with Central Bank	-	45,115		-	45,115
Securities	-	93,976	249	-	94,225
Due from credit institutions	-	65,334	253	-	65,587
Due from other segments	31,082	24,965	111	(56,158)	-
Loans to customers	92,768	554,156	95,462	-	742,386
Loans to other segments	-	79,651	-	(79,651)	-
Other assets	184	15,378	6,147	-	21,709
Other assets to other segments	-	1,347	-	(1,347)	-
Total assets	**124,034**	**879,922**	**102,222**	**(137,156)**	**969,022**
Reportable segment liabilities and shareholder's equity	**124,034**	**879,922**	**102,222**	-	**-**
Segment liabilities comprise:					
Due to credit institutions	82,051	413,876	19,301	-	515,228
Due to other segments	15,716	31,082	79,651	(126,449)	-
Due to customers	-	302,098	-	-	302,098
Due to other segments (deposits)	-	111	-	(111)	-
Issued debt securities	-	40,660	-	-	40,660
Other liabilities	10,722	7,367	1,432	-	19,521
Other liabilities to segments	9,249	-	301	(9,550)	-
Subordinated liabilities	-	31,089	-	-	31,089
Shareholders equity	6,296	53,639	491	-	60,426
Shareholders equity to other segments	-		1,046	(1,046)	-
Total liabilities and shareholder's equity	**124,034**	**879,922**	**102,222**	**(137,156)**	**969,022**

NOTES TO THE FINANCIAL STATEMENTS

35 OFF BALANCE SHEET ITEMS AND CONTINGENT LIABILITIES

	31/12/09		31/12/08	
	Group	**Bank**	**Group**	**Bank**
Contingent liabilities				
outstanding guarantees	12,080	14,194	24,007	24,007
Financial commitments				
unutilised loan facilities	32,685	55,077	29,448	39,101
Other liabilities	252	252	298	298
Total	**45,017**	**69,523**	**53,753**	**63,406**

36 MAXIMUM EXPOSURE TO CREDIT RISK

The table below shows credit risk exposures relating to on-balance sheet assets and off-balance sheet items before collateral held or other credit enhancements:

	31/12/09		31/12/08	
	Group	**Bank**	**Group**	**Bank**
Credit risk exposures relating to on-balance sheet assets are as follows:				
Trading securities	5,074	4,919	3,859	3,711
Investment securities – held to maturity	42,984	42,984	64,070	63,969
Investment securities – available for sale	49,892	49,892	26,296	26,296
Due from credit institutions	35,411	35,276	65,587	65,334
Derivative financial instruments	1,954	1,954	1,581	1,581
Loans to customers	632,681	639,501	742,386	726,575
Other assets	8,896	1,865	5,000	1,456
Total	**776,892**	**776,391**	**908,779**	**888,922**
Credit risk exposures relating to off-balance sheet items are as follows:				
Contingent liabilities	12,080	14,194	24,007	24,007
Financial commitments	32,937	55,329	29,746	39,399
Total	**45,017**	**69,523**	**53,753**	**63,406**

37 FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES

In respect of financial assets and liabilities held in the Group's balance sheet at carrying values other than fair value, in the opinion of Management the fair value of those financial assets and liabilities differ from their carrying values, as follows:

	31/12/09		31/12/08	
	Book value	**Fair value**	**Book value**	**Fair value**
Assets				
Due from credit institutions	35,411	35,410	65,587	65,578
Loans to customers	632,681	634,321	742,386	732,785
Investment securities held to maturity	42,984	43,138	64,070	62,792
Liabilities				
Due to credit institutions	379,512	379,511	515,228	515,228
Due to customers	324,749	324,027	302,098	301,197
Mortgage bonds	37,429	37,011	40,660	40,678

NOTES TO THE FINANCIAL STATEMENTS

37 FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES (continued)

In assessing the differences of fair value to carrying value, management has performed discounted cash flow analysis where financial assets and liabilities are at fixed rates of interest for fixed period. All items where interest rates are pegged to floating market interest rates have not been recalculated; the carrying value is considered equal to fair value.

Fair value hierarchy:

The Bank classifies the fair value measurements using fair value hierarchy reflecting importance of the data used in the assessment. The Bank uses 3-level fair value hierarchy:

- Level 1. If there is active market for the financial asset, the Bank uses the latest available market prices of the financial asset. The market price of the financial instruments is obtained from the stock exchange or reliable information systems (*Reuters, Bloomberg*,) depending on the Bank's procedure for choosing the source of the market price.
- Level 2. If the trade price of the financial asset is not easily and regularly available or if there is no active market for the financial asset, the active market is lost or there is impartial evidence that the quotations do not show the actual value of the financial asset, the Bank uses discounted cash flow technique assuming the market rate is the discount rate based on analysis of the information published in the active market. The Bank defines the market rate using the valuation methods of experts based on active market prices of the financial asset, some of its components or similar instruments having identical terms and characteristics (region, sector, maturity, currency, cover, credit ratings).
- Level 3. If the financial asset does not have active market and there is no market information available for determination of market rate, the Bank derives and substantiates the market rate of the financial asset using data not based on the market information.

Group's financial assets measured at fair value by fair value hierarchy:

	31/12/09			
	Level 1	**Level 2**	**Level 3**	**Total**
Financial assets held for sale				
Debt securities	4,709	-	305	**5,014**
Shares	60	-	-	**60**
Derivative financial instruments	1,954	-	-	**1,954**
Financial assets – available for sale				
Debt securities	49,892	-	-	**49,892**

38 CONTINGENT LIABILITIES

The tax authorities may at any time inspect the books and records within 3 years subsequent to the reported tax year and may impose additional tax assessments and penalties, if any. The Group's management is not aware of any circumstances which may give rise to a potential material liability in this respect.

39 MOVEMENT IN REVALUTION RESERVE OF INVESTMENT SECURITIES AVAILABLE FOR SALE

	2009		2008	
	Group	**Bank**	**Group**	**Bank**
At 1 January	(3,562)	(3,562)	(1,540)	(1,540)
Net profit / (losses) from changes in fair value	528	528	(2,022)	(2,022)
At 31 December	**(3,034)**	**(3,034)**	**(3,562)**	**(3,562)**

NOTES TO THE FINANCIAL STATEMENTS

40 MATURITY ANALYSIS OF ASSETS AND LIABILITIES

The table below allocates the Group's assets and liabilities to maturity groupings as at 31 December 2009 based on the time remaining from the balance sheet date to the contractual maturity dates.

	Up to 1 month	1 to 3 months	3 to 6 months	6 to 12 months	1 to 5 years	Over 5 years and undated	**Total**
ASSETS							
Cash and balances with the Central Bank	95,997	-	-	-	-	-	**95,997**
Securities	3,984	31,020	18,288	5,990	32,675	5,993	**97,950**
Investment properties	-	-	-	-	-	1,166	**1,166**
Due from credit institutions	33,159	12	1,949	28	263	-	**35,411**
Loans to customers	40,973	30,428	33,422	64,989	254,548	208,321	**632,681**
Derivative financial instruments	1,233	721	-	-	-	-	**1,954**
Investment in subsidiaries and associated undertakings	-	-	-	-	-	280	**280**
Intangible assets	-	-	-	-	-	2,204	**2,204**
Property and equipment	-	-	-	-	-	7,536	**7,536**
Other assets	-	-	-	-	-	8,896	**8,896**
Deferred expenses and accrued income	-	-	-	-	-	662	**662**
Total assets	**175,346**	**62,181**	**53,659**	**71,007**	**287,486**	**235,058**	**884,737**
LIABILITIES AND SHAREHOLDERS EQUITY							
Due to credit institutions*	21,959	5,885	28,817	123,535	136,676	62,640	**379,512**
Due to customers	148,045	52,181	51,924	63,166	8,815	618	**324,749**
Derivative financial instruments	68	87	-	-	-	-	**155**
Transit funds	-	-	169	163	1,423	195	**1,950**
Mortgage bonds	-	687	-	3,001	33,741	-	**37,429**
Other liabilities	-	-	-	-	-	27,400	**27,400**
Deferred income and accrued expenses	-	-	-	-	-	3,997	**3,997**
Current income tax liabilities	-	-	-	-	-	43	**43**
Deferred tax liabilities	-	-	-	-	-	27	**27**
Subordinated debt	-	-	5	-	10,000	21,084	**31,089**
Shareholder's equity	-	-	-	-	-	78,386	**78,386**
Total liabilities and shareholder's equity	**170,072**	**58,840**	**80,915**	**189,865**	**190,655**	**194,390**	**884,737**
Net liquidity	**5,274**	**3,341**	**(27,256)**	**(118,858)**	**96,831**	**40,668**	**-**
As at 31 December 2008							
Total assets	**106,957**	**45,735**	**58,529**	**108,017**	**286,958**	**362,826**	**969,022**
Total liabilities and shareholder's equity	**140,943**	**51,971**	**82,006**	**200,902**	**348,465**	**144,735**	**969,022**
Net liquidity	**(33,986)**	**(6,236)**	**(23,477)**	**(92,885)**	**(61,507)**	**218,091**	**-**

NOTES TO THE FINANCIAL STATEMENTS

40 MATURITY ANALYSIS OF ASSETS AND LIABILITIES (continued)

The table below allocates the Bank's assets and liabilities to maturity groupings as at 31 December 2009 based on the time remaining from the balance sheet date to the contractual maturity dates.

	Up to 1 month	1 to 3 months	3 to 6 months	6 to 12 months	1 to 5 years	Over 5 years and undated	**Total**
ASSETS							
Cash and balances with the Central Bank	95,997	-	-	-	-	-	**95,997**
Securities	3,829	31,020	18,288	5,990	32,675	5,993	**97,795**
Investment properties	-	-	-	-	-	1,166	**1,166**
Due from credit institutions	33,024	12	1,949	28	263	-	**35,276**
Loans to customers	37,583	27,157	28,860	54,744	283,497	207,660	**639,501**
Derivative financial instruments	1,233	721	-	-	-	-	**1,954**
Investment in subsidiaries and associated undertakings	-	-	-	-	-	1,528	**1,528**
Intangible assets	-	-	-	-	-	1,721	**1,721**
Property and equipment	-	-	-	-	-	6,896	**6,896**
Other assets	-	-	-	-	-	1,865	**1,865**
Deferred expenses and accrued income	-	-	-	-	-	532	**532**
Total assets	**171,666**	**58,910**	**49,097**	**60,762**	**316,435**	**227,361**	**884,231**
LIABILITIES AND SHAREHOLDERS EQUITY							
Due to credit institutions*	21,959	5,885	28,817	123,535	136,676	62,640	**379,512**
Due to customers	148,107	52,181	51,924	63,166	8,815	618	**324,811**
Derivative financial instruments	68	87	-	-	-	-	**155**
Transit funds	-	-	169	163	1,423	195	**1,950**
Mortgage bonds	-	687	-	3,001	34,561	-	**38,249**
Other liabilities	-	-	-	-	-	26,835	**26,835**
Deferred income and accrued expenses	-	-	-	-	-	3,376	**3,376**
Current income tax liabilities	-	-	-	-	-	-	**-**
Deferred tax liabilities	-	-	-	-	-	-	**-**
Subordinated debt	-	-	5	-	10,000	21,084	**31,089**
Shareholder's equity	-	-	-	-	-	78,254	**78,254**
Total liabilities and shareholder's equity	**170,134**	**58,840**	**80,915**	**189,865**	**191,475**	**193,002**	**884,231**
Net liquidity	**1,532**	**70**	**(31,818)**	**(129,103)**	**124,960**	**34,359**	**-**
As at 31 December 2008							
Total assets	**104,072**	**41,922**	**55,073**	**96,713**	**294,915**	**355,214**	**947,909**
Total liabilities and shareholder's equity	**141,054**	**51,645**	**82,006**	**181,927**	**348,465**	**142,812**	**947,909**
Net liquidity	**(36,982)**	**(9,723)**	**(26,933)**	**(85,214)**	**(53,550)**	**212,402**	**-**

* Due to credit institutions comprise syndicated loans from the lenders who had not yet made the formal changes to the agreements as at 31 December 2009 and which as at 31 December 2009 amount to 70,133 thousand LVL. These syndicated loans are included in the maturity grouping according to the original payment terms set in the agreements (see Note 25).

NOTES TO THE FINANCIAL STATEMENTS

40 MATURITY ANALYSIS OF ASSETS AND LIABILITIES (continued)

The table below allocates undiscounted future cash flows of the Group's financial liabilities and liquid assets as at 31 December 2009:

	Up to 1 month	1 to 3 months	3 to 6 months	6 to 12 months	1 to 5 years	Over 5 years and undated	**Total**
Due to credit institutions	23,359	6,912	31,687	126,055	149,843	66,772	**404,628**
Due to customers	148,375	53,248	53,514	65,488	9,495	620	**330,740**
Transit funds	-	-	183	184	1,518	197	**2,082**
Mortgage bonds	-	917	-	3,917	36,992	-	**41,826**
Other liabilities	-	-	-	-	-	27,400	**27,400**
Subordinated debt	-	-	894	909	16,142	21,389	**39,334**
Total financial liabilities	**171,734**	**61,077**	**86,278**	**196,553**	**213,990**	**116,378**	**846,010**
Liquid assets	**129,686**	**31,547**	**11,910**	**1,025**	**12,309**	**4,158**	**190,635**

The table below allocates undiscounted future cash flows of the Bank's financial liabilities and liquid assets as at 31 December 2009:

	Up to 1 month	1 to 3 months	3 to 6 months	6 to 12 months	1 to 5 years	Over 5 years and undated	**Total**
Due to credit institutions	23,359	6,912	31,687	126,055	149,843	66,772	**404,628**
Due to customers	148,437	53,248	53,514	65,488	9,495	620	**330,802**
Transit funds	-	-	183	184	1,518	197	**2,082**
Mortgage bonds	-	937	-	3,937	37,857	-	**42,731**
Other liabilities	-	-	-	-	-	26,835	**26,835**
Subordinated debt	-	-	894	909	16,142	21,389	**39,334**
Total financial liabilities	**171,796**	**61,097**	**86,278**	**196,573**	**214,855**	**115,813**	**846,412**
Liquid assets	**129,396**	**31,547**	**11,910**	**1,025**	**12,309**	**4,158**	**190,345**

The table below allocates undiscounted future cash flows of the Group's financial liabilities and liquid assets as at 31 December 2008:

	Up to 1 month	1 to 3 months	3 to 6 months	6 to 12 months	1 to 5 years	Over 5 years and undated	**Total**
Due to credit institutions	15,786	9,064	24,592	149,250	321,943	48,000	**568,635**
Due to customers	125,633	45,290	64,762	61,143	11,131	541	**308,500**
Transit funds	-	-	227	226	1,724	609	**2,786**
Mortgage bonds	-	1,201	-	4,201	44,011	-	**49,413**
Other liabilities	-	-	-	-	-	13,083	**13,083**
Subordinated debt	-	-	895	948	16,710	22,624	**41,177**
Total financial liabilities	**141,419**	**55,555**	**90,476**	**215,768**	**395,519**	**84,857**	**983,594**
Liquid assets	**76,615**	**11,307**	**3,064**	**2,826**	**14,464**	**5,522**	**113,798**

NOTES TO THE FINANCIAL STATEMENTS

40 MATURITY ANALYSIS OF ASSETS AND LIABILITIES (continued)

The table below allocates undiscounted future cash flows of the Bank's financial liabilities and liquid assets as at 31 December 2008:

	Up to 1 month	1 to 3 months	3 to 6 months	6 to 12 months	1 to 5 years	Over 5 years and undated	**Total**
Due to credit institutions	15,786	8,510	24,592	129,720	321,943	48,000	**548,551**
Due to customers	125,744	45,290	64,762	61,143	11,131	541	**308,611**
Transit funds	-	-	227	226	1,724	609	**2,786**
Mortgage bonds	-	1,201	-	4,201	44,011	-	**49,413**
Other liabilities	-	-	-	-	-	12,379	**12,379**
Subordinated debt	-	-	895	948	16,710	22,624	**41,177**
Total financial liabilities	**141,530**	**55,001**	**90,476**	**196,238**	**395,519**	**84,153**	**962,917**
Liquid assets	**76,214**	**11,307**	**3,064**	**2,826**	**14,464**	**5,522**	**113,397**

The table below allocates the Group's derivative future cash flows as at 31 December 2009:

	Up to 1 month	1 to 3 months	3 to 6 months	6 to 12 months	1 to 5 years	Over 5 years	**Total**
Derivatives settled on a gross basis							
Foreign exchange derivatives							
outflow	54,323	33,370	-	-	-	-	**87,693**
inflow	55,503	34,086	-	-	-	-	**89,589**

The table below allocates the Bank's derivative future cash flows as at 31 December 2009:

	Up to 1 month	1 to 3 months	3 to 6 months	6 to 12 months	1 to 5 years	Over 5 years	**Total**
Derivatives settled on a gross basis							
Foreign exchange derivatives							
outflow	54,323	33,370	-	-	-	-	**87,693**
inflow	55,503	34,086	-	-	-	-	**89,589**

The table below allocates the Group's derivative future cash flows as at 31 December 2008:

	Up to 1 month	1 to 3 months	3 to 6 months	6 to 12 months	1 to 5 years	Over 5 years	**Total**
Derivatives settled on a gross basis							
Foreign exchange derivatives							
outflow	22,644	17,453	63,927	9,779	-	-	**113,803**
inflow	22,961	18,418	64,905	10,000	-	-	**116,284**

The table below allocates the Bank's derivative future cash flows as at 31 December 2008:

	Up to 1 month	1 to 3 months	3 to 6 months	6 to 12 months	1 to 5 years	Over 5 years	**Total**
Derivatives settled on a gross basis							
Foreign exchange derivatives							
outflow	22,644	17,453	63,927	9,779	-	-	**113,803**
inflow	22,961	18,418	64,905	10,000	-	-	**116,284**

NOTES TO THE FINANCIAL STATEMENTS

41 RE-PRICING MATURITY ANALYSIS

The table below allocates the Group's assets and liabilities to maturity groupings as at 31 December 2009 based on the time remaining from the balance sheet date to the earlier of maturity and contractual re-pricing dates.

	Up to 1 month	1 to 3 month	3 to 6 month	6 to 12 month	1 to 5 years	Over 5 years	Non-interest bearing	**Total**
ASSETS								
Cash and balances with the Central Bank	95,997	-	-	-	-	-	-	**95,997**
Securities	9,817	37,500	18,420	3,392	23,131	5,630	60	**97,950**
Investment properties	-	-	-	-	-	-	1,166	**1,166**
Due from credit institutions	35,411	-	-	-	-	-	-	**35,411**
Loans to customers	170,638	153,425	184,899	30,956	82,962	9,801	-	**632,681**
Derivative financial instruments	1,233	721	-	-	-	-	-	**1,954**
Investment in subsidiaries and associated undertakings	-	-	-	-	-	-	280	**280**
Intangible assets	-	-	-	-	-	-	2,204	**2,204**
Property and equipment	-	-	-	-	-	-	7,536	**7,536**
Other assets	-	-	-	-	-	-	8,896	**8,896**
Deferred expenses and accrued income	-	-	-	-	-	-	662	**662**
Total assets	**313,096**	**191,646**	**203,319**	**34,348**	**106,093**	**15,431**	**20,804**	**884,737**
LIABILITIES AND SHAREHOLDERS EQUITY								
Due to credit institutions	137,444	131,268	110,800	-	-	-	-	**379,512**
Due to customers	148,045	52,181	51,924	63,166	8,815	618	-	**324,749**
Derivative financial instruments	68	87	-	-	-	-	-	**155**
Transit funds	-	-	1,950	-	-	-	-	**1,950**
Mortgage bonds	-	19,659			17,770		-	**37,429**
Other liabilities	-	-	-	-	-	-	27,400	**27,400**
Deferred income and accrued expenses	-	-	-	-	-	-	3,997	**3,997**
Current income tax liabilities	-	-	-	-	-	-	43	**43**
Deferred tax liability	-	-	-	-	-	-	27	**27**
Subordinated debt	-	-	5	-	10,000	21,084	-	**31,089**
Shareholder's equity	-	-	-	-	-	-	78,386	**78,386**
Total liabilities and shareholder's equity	**285,557**	**203,195**	**164,679**	**63,166**	**36,585**	**21,702**	**109,853**	**884,737**
On balance sheet interest sensitivity analysis	**27,539**	**(11,549)**	**38,640**	**(28,818)**	**69,508**	**(6,271)**	**(89,049)**	**-**
As at 31 December 2008								
Total assets	**298,141**	**192,021**	**233,414**	**54,601**	**147,273**	**23,385**	**20,187**	**969,022**
Total liabilities and shareholder's equity	**273,795**	**344,361**	**154,459**	**59,278**	**38,380**	**21,624**	**77,125**	**969,022**
On balance sheet interest sensitivity analysis	**24,346**	**(152,340)**	**78,955**	**(4,677)**	**108,893**	**1,761**	**(56,938)**	**-**

NOTES TO THE FINANCIAL STATEMENTS

41 RE-PRICING MATURITY ANALYSIS (continued)

The table below allocates the Bank's assets and liabilities to maturity groupings as at 31 December 2009 based on the time remaining from the balance sheet date to the earlier of maturity and contractual re-pricing dates.

	Up to 1 month	1 to 3 month	3 to 6 month	6 to 12 month	1 to 5 years	Over 5 years	Non-interest bearing	**Total**
ASSETS								
Cash and balances with the Central Bank	95,997	-	-	-	-	-	-	**95,997**
Securities	9,662	37,500	18,420	3,392	23,131	5,630	60	**97,795**
Investment properties	-	-	-	-	-	-	1,166	**1,166**
Due from credit institutions	35,276	-	-	-	-	-	-	**35,276**
Loans to customers	174,177	155,875	184,773	30,767	84,111	9,798	-	**639,501**
Derivative financial instruments	1,233	721	-	-	-	-	-	**1,954**
Investment in subsidiaries and associated undertakings	-	-	-	-	-	-	1,528	**1,528**
Intangible assets	-	-	-	-	-	-	1,721	**1,721**
Property and equipment	-	-	-	-	-	-	6,896	**6,896**
Other assets	-	-	-	-	-	-	1,865	**1,865**
Deferred expenses and accrued income	-	-	-	-	-	-	532	**532**
Total assets	**316,345**	**194,096**	**203,193**	**34,159**	**107,242**	**15,428**	**13,768**	**884,231**
LIABILITIES AND SHAREHOLDERS EQUITY								
Due to credit institutions	137,444	131,268	110,800	-	-	-	-	**379,512**
Due to customers	148,107	52,181	51,924	63,166	8,815	618	-	**324,811**
Derivative financial instruments	68	87	-	-	-	-	-	**155**
Transit funds	-		1,950	-	-	-	-	**1,950**
Mortgage bonds	-	19,848		-	18,401	-	-	**38,249**
Other liabilities	-	-	-	-	-	-	26,835	**26,835**
Deferred income and accrued expenses	-	-	-	-	-	-	3,376	**3,376**
Current income tax liabilities	-	-	-	-	-	-	-	**-**
Deferred tax liability	-	-	-	-	-	-	-	**-**
Subordinated debt	-	-	5	-	10,000	21,084	-	**31,089**
Shareholder's equity	-	-	-	-	-	-	78,254	**78,254**
Total liabilities and shareholder's equity	**285,619**	**203,384**	**164,679**	**63,166**	**37,216**	**21,702**	**108,465**	**884,231**
On balance sheet interest sensitivity analysis	**30,726**	**(9,288)**	**38,514**	**(29,007)**	**70,026**	**(6,274)**	**(94,697)**	**-**
As at 31 December 2007								
Total assets	**282,607**	**192,382**	**233,227**	**54,379**	**146,545**	**23,382**	**15,387**	**947,909**
Total liabilities and shareholder's equity	**273,906**	**325,060**	**154,459**	**59,278**	**38,380**	**21,624**	**75,202**	**947,909**
On balance sheet interest sensitivity analysis	**8,701**	**(132,678)**	**78,768**	**(4,899)**	**108,165**	**1,758**	**(59,815)**	**-**

NOTES TO THE FINANCIAL STATEMENTS

42 CURRENCY ANALYSIS OF ASSETS AND LIABILITIES

The following table provides the analysis of the Group's assets, liabilities and shareholders' equity as well as memorandum items outstanding as at 31 December 2009 by currency profile:

	LVL	USD	EUR	Other	**Total**
ASSETS					
Cash and balances with the Central Bank	93,024	571	1,636	766	**95,997**
Securities	54,658	7,671	35,620	1	**97,950**
Investment properties	1,166	-	-	-	**1,166**
Due from credit institutions	17,173	3,536	14,519	183	**35,411**
Loans to customers	54,879	6,586	570,598	618	**632,681**
Derivative financial instruments	1,954	-	-	-	**1,954**
Investment in subsidiaries and associated undertakings	280	-	-	-	**280**
Intangible assets	2,204	-	-	-	**2,204**
Property and equipment	7,536	-	-	-	**7,536**
Other assets	1,470	38	7,371	17	**8,896**
Deferred expenses and accrued income	556	-	106	-	**662**
Total assets	**234,900**	**18,402**	**629,850**	**1,585**	**884,737**
LIABILITIES AND SHAREHOLDERS EQUITY					
Due to credit institutions	16,533	1,667	361,312	-	**379,512**
Due to customers	142,717	20,057	161,482	493	**324,749**
Derivative financial instruments	155	-	-	-	**155**
Transit funds	353	-	1,597	-	**1,950**
Mortgage bonds	12,468	2,747	22,214	-	**37,429**
Other liabilities	24,449	6	2,945	-	**27,400**
Deferred income and accrued expenses	2,612	-	1,385	-	**3,997**
Current income tax liabilities	43	-	-	-	**43**
Deferred tax liabilities	27	-	-	-	**27**
Subordinated debt	10,002	-	21,087	-	**31,089**
Shareholders equity	78,386	-	-	-	**78,386**
Total liabilities and shareholder's equity	**287,745**	**24,477**	**572,022**	**493**	**884,737**
Spot foreign exchange receivables / (payables)	(4,254)	-	2,881	(71)	(1,444)
Forward foreign exchange receivables / (payables)	63,136	6,135	(66,668)	(708)	1,895
Currency position	**6,037**	**60**	**(5,959)**	**313**	**451**
As at 31 December 2008					
Total assets	**221,276**	**41,145**	**704,340**	**2,261**	**969,022**
Total liabilities and shareholder's equity	**281,255**	**26,179**	**661,242**	**346**	**969,022**
Spot foreign exchange receivables / (payables)	(562)	-	563	-	1
Forward foreign exchange receivables / (payables)	69,939	(15,347)	(50,613)	(1,498)	2,481
Currency position	**9,398**	**(381)**	**(6,952)**	**417**	**2,482**

NOTES TO THE FINANCIAL STATEMENTS

42 CURRENCY ANALYSIS OF ASSETS AND LIABILITIES (continued)

The following table provides the analysis of the Bank's assets, liabilities and shareholders' equity as well as memorandum items outstanding as at 31 December 2009 by currency profile:

	LVL	USD	EUR	Other	**Total**
ASSETS					
Cash and balances with the Central Bank	93,024	571	1,636	766	**95,997**
Securities	54,658	7,671	35,465	1	**97,795**
Investment properties	1,166	-	-	-	**1,166**
Due from credit institutions	17,076	3,534	14,483	183	**35,276**
Loans to customers	54,264	6,736	577,883	618	**639,501**
Derivative financial instruments	1,954	-	-	-	**1,954**
Investment in subsidiaries and associated undertakings	1,528	-	-	-	**1,528**
Intangible assets	1,721	-	-	-	**1,721**
Property and equipment	6,896	-	-	-	**6,896**
Other assets	1,358	38	452	17	**1,865**
Deferred expenses and accrued income	426	-	106	-	**532**
Total assets	**234,071**	**18,550**	**630,025**	**1,585**	**884,231**
LIABILITIES AND SHAREHOLDERS EQUITY					
Due to credit institutions	16,533	1,667	361,312	-	**379,512**
Due to customers	142,770	20,059	161,489	493	**324,811**
Derivative financial instruments	155	-	-	-	**155**
Transit funds	353	-	1,597	-	**1,950**
Mortgage bonds	12,468	2,952	22,829	-	**38,249**
Other liabilities	24,201	6	2,628	-	**26,835**
Deferred income and accrued expenses	2,098	-	1,278	-	**3,376**
Current income tax liabilities	-	-	-	-	**-**
Deferred tax liabilities	-	-	-	-	**-**
Subordinated debt	10,002	-	21,087	-	**31,089**
Shareholders equity	78,254	-	-	-	**78,254**
Total liabilities and shareholder's equity	**286,834**	**24,684**	**572,220**	**493**	**884,231**
Spot foreign exchange receivables/ (payables)	(4,254)	-	2,881	(71)	(1,444)
Forward foreign exchange receivables / (payables)	63,136	6,135	(66,668)	(708)	1,895
Currency position	**6,119**	**1**	**(5,982)**	**313**	**451**
As at 31 December 2008					
Total assets	**216,718**	**41,094**	**687,836**	**2,261**	**947,909**
Total liabilities and shareholder's equity	**279,759**	**26,179**	**641,625**	**346**	**947,909**
Spot foreign exchange receivables / (payables)	(562)	-	563	-	1
Forward foreign exchange receivables / (payables)	69,939	(15,347)	(50,613)	(1,498)	2,481
Currency position	**6,336**	**(432)**	**(3,839)**	**417**	**2,482**

NOTES TO THE FINANCIAL STATEMENTS

43 CAPITAL ADEQUACY CALCULATION

Based on the requirements set by the Financial and Capital Market Commission (FCMC), the Group's and the Bank's equity to be utilised in the capital adequacy ratio as at 31 December 2009 has been calculated as follows:

	31/12/2009	
	Group	**Bank**
Tier 1		
- paid-in share capital	121,321	121,321
- legal and other reserves	2,553	2,063
- audited retained earnings	11,423	11,422
- loss for the period	(54,410)	(54,051)
- negative revaluation reserve on investment securities available-for-sale	(3,034)	(3,034)
- intangible assets	(2,204)	(1,721)
Total Tier 1	**75,649**	**76,000**
Tier 2		
- subordinated capital (restricted to 50% of Tier 1)	31,084	31,084
- decrease of subordinated capital	(4,000)	(4,000)
Total Tier 2	**27,084**	**27,084**
Capital base	**102,733**	**103,084**

The total of Tier 2 may not exceed the total of Tier 1.

NOTES TO THE FINANCIAL STATEMENTS

43 CAPITAL ADEQUACY CALCULATION (continued)

The following table shows the Group's asset weightings used in calculation of capital adequacy ratio according to the FCMC requirements and calculation of the Group's capital adequacy ratio according to the FCMC requirements:

	Credit equivalent	Balance	Risk weighted assets
Assets and off-balance sheet items			
Claims or contingent claims on central governments or central banks		150,027	1,934
Claims or contingent claims on regional governments or local authorities		600	600
Claims or contingent claims on institutions		58,175	22,709
Claims in the form of covered bonds		8,924	4,462
Claims or contingent claims on corporates		595,231	575,058
Past due items		86,765	110,713
Other claims		25,874	20,955
Derivative financial instruments	766	1,954	551
Deductions from capital:			
Intangible assets		2,204	-
Total assets and off-balance sheet items		**929,754**	**736,982**
Calculation of capital requirements			
Capital requirement for the Group's portfolio credit risk	8%		58,959
Operational risk capital requirement			4,338
Capital requirements for market risk			528
Capital requirement for the Group's portfolio credit risk and market risk			**63,825**
Capital base			**102,733**
Capital adequacy ratio (Capital base / Capital requirement x 8%)			**12.9%**

NOTES TO THE FINANCIAL STATEMENTS

43 CAPITAL ADEQUACY CALCULATION (continued)

The following table shows the Bank's asset weightings used in calculation of capital adequacy ratio according to the FCMC requirements and calculation of the Bank's capital adequacy ratio according to the FCMC requirements:

	Credit equivalent	Balance	Risk weighted assets
Assets and off-balance sheet items			
Claims or contingent claims on central governments or central banks		150,027	1,934
Claims or contingent claims on regional governments or local authorities		600	600
Claims or contingent claims on institutions		57,886	22,419
Claims in the form of covered bonds		8,924	4,462
Claims or contingent claims on corporates		630,206	595,838
Past due items		86,765	110,713
Other claims		19,557	14,637
Derivative financial instruments	766	1,954	551
Deductions from capital:			
Intangible assets		1,721	-
Total assets and off-balance sheet items		**957,640**	**751,154**
Calculation of capital requirements			
Capital requirement for the Group's portfolio credit risk	8%		60,092
Operational risk capital requirement			4,027
Capital requirements for market risk			444
Capital requirement for the Group's portfolio credit risk and market risk			**64,563**
Capital base			**103,084**
Capital adequacy ratio (Capital base / Capital requirement x 8%)			**12.8%**

44 FUTURE MINIMUM LEASE PAYMENTS FOR OPERATIONAL LEASES

The following table discloses future minimum lease payments for premises operational leases (other lease payments also exist while those are comparatively small):

	Group	**Bank**
Year 2010	832	775
Year 2011	662	605
Year 2012	455	417
Year 2013	385	385
Year 2014 and later	4,088	4,088
Total	**6,422**	**6,270**

NOTES TO THE FINANCIAL STATEMENTS

45 ANALYSIS OF FINANCIAL ASSETS AND LIABILITIES BY MEASUREMENT

The assets and liabilities of the Group as at 31 December 2009 by measurement are as follows:

	Held to trading	Available for sale	Amortised cost	Total book value
ASSETS				
Cash and balances with the Central Bank	-	-	95,997	**95,997**
Securities	5,074	49,892	42,984	**97,950**
Investment properties	1,166	-	-	**1,166**
Due from credit institutions	-	-	35,411	**35,411**
Loans to customers	-	-	632,681	**632,681**
Derivative financial instruments	1,954	-	-	**1,954**
Other financial assets	-	-	2,244	**2,244**
Total financial assets	**8,194**	**49,892**	**809,317**	**867,403**
Non-financial assets	-	-	-	**17,334**
Total assets	**8,194**	**49,892**	**809,317**	**884,737**
LIABILITIES				
Due to credit institutions	-	-	379,512	**379,512**
Due to customers	-	-	324,749	**324,749**
Derivative financial instruments	155	-	-	**155**
Transit funds	-	-	1,950	**1,950**
Mortgage bonds	-	-	37,429	**37,429**
Subordinated liabilities	-	-	31,089	**31,089**
Other financial liabilities	-	-	27,400	**27,400**
Total financial liabilities	**155**	**-**	**802,129**	**802,284**
Non-financial liabilities	-	-	-	**82,453**
Total liabilities	**155**	**-**	**802,129**	**884,737**

NOTES TO THE FINANCIAL STATEMENTS

45 ANALYSIS OF FINANCIAL ASSETS AND LIABILITIES BY MEASUREMENT (continued)

The assets and liabilities of the Bank as at 31 December 2009 by measurement are as follows:

	Held to trading	Available for sale	Amortised cost	Total book value
ASSETS				
Cash and balances with the Central Bank	-	-	95,997	**95,997**
Securities	4,919	49,892	42,984	**97,795**
Investment properties	1,166	-	-	**1,166**
Due from credit institutions	-	-	35,276	**35,276**
Loans to customers	-	-	639,501	**639,501**
Derivative financial instruments	1,954	-	-	**1,954**
Other financial assets	-	-	1,736	**1,736**
Total financial assets	**8,039**	**49,892**	**815,494**	**873,425**
Non-financial assets	-	-	-	**10,806**
Total assets	**8,039**	**49,892**	**815,494**	**884,231**
LIABILITIES				
Due to credit institutions	-	-	379,512	**379,512**
Due to customers	-	-	324,811	**324,811**
Derivative financial instruments	155	-	-	**155**
Transit funds	-	-	1,950	**1,950**
Mortgage bonds	-	-	38,249	**38,249**
Subordinated liabilities	-	-	31,089	**31,089**
Other financial liabilities	-	-	26,835	**26,835**
Total financial liabilities	**155**	**-**	**802,446**	**802,601**
Non-financial liabilities	-	-	-	**81,630**
Total liabilities	**155**	**-**	**802,446**	**884,231**