Joint Stock Company **Parex banka**

PAREX BANKA

Unaudited

Public Financial Report

For the 1st half of 2011

MAXIMUM RECOVERY OF STATE AID

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Management report

Dear Shareholders and Collaboration Partners,

The biggest and most important challenge for Parex banka during the first six months of 2011 was repayment of the State guaranteed international syndicated loan in the amount of 164 million lats. We are pleased to announce that persistent hard work of the Bank's management and the employee team has resulted in accomplishing this goal. Therefore we were able to defend the interests of the state tax payers by completely settling the most important liabilities of Parex banka without additional State Aid. The accomplishment is also a positive signal for foreign investors and rating agencies, and it once again underlines the correctness of the strategy selected by the Latvian government with regard to solving the problems of Latvia's banking sector. It is no secret that many important participants of international financial markets observed us with great interest for they saw fulfilment of the substantial loan liabilities as a significant indicator of Latvia's economic recovery. The funds necessary for repayment of the syndicated loan were recovered from restructuring problematic loans contained in Parex banka's asset portfolio as well as from selling securities and utilising the cost resources that Parex banka had accrued. This enabled us to have absolute faith in the fact that there will be enough funds for duly settling accounts with the lender and for continuing the Bank's business activity.

In accordance with the restructuring plan for Parex banka approved by the European Commission and the Cabinet of Ministers, we continued recovering the Bank's assets, and repossessing, overtaking and professionally managing real estate, during the accounting period. Since the split-up of the Bank we have taken over approximately 800 real estate objects and we anticipate that this number will significantly increase during 2011. The Bank's real estate portfolio consists of assets of various types and quality and therefore its future value potential is equally diverse. We carry out a detailed analysis of each asset. Including applying prognoses for economic growth perspectives, development of the real estate market, cash flows that the corresponding object may generate as well as other important factors elaborated by the Bank's experts. As a result, we adopt a decision on selling the asset in question, or, renting it out until a more beneficial situation occurs in the market. To ensure maximum transparency of decisions adopted and transactions affected by the Bank, we require an assessment made by independent experts in the corresponding field, thus exercising the so called “four eyes” principle. Even though, in essence, it would be enough to rely solely on the analysis carried out by the Bank’s experts, Parex banka’s continuing to be a focal point of society’s and supervising authorities’ attention leads to the necessity for exercise this principle. We are aware that there is a good reason for interest expressed toward Parex banka: our work results influence each and every one of Latvia’s tax payers and the State as such since the reason for the Bank’s existence is recovery of State investments in the maximum amount possible.

During the accounting period, Parex banka’s business activity has been conducted closely in line with the budget for 2011 and with the restructuring plan. We have recovered over 100 million Lats during the accounting period, channelling the majority of these funds for repayment of the syndicated loan. In accordance with the requirements of International Financial Reporting Standards and the cautious accountancy policy exercised by Parex banka, accruals for doubtful loans in the amount of 18.6 million Lats during the first six months of this year. Even though these accruals are disclosed as losses in the Bank’s balance sheet, the consistent policy for developing accruals ensures additional security in the difficult economic circumstances, thus this is a positive aspect. Depending on further development scenarios for Latvia and the global economy which may leave a significant impact on recovering certain loans, the recognized amount of accruals may be reviewed and decreased in case of a beneficial situation. Likewise, interest payments, which in accordance with the provisions of the agreement, Parex banka has to repay to the State budget for the investments are also disclosed as expenses in the Bank’s profit and loss statement. Correspondingly, after the end of the accounting period, the State Treasury will be supplemented with a significant sum of money, i.e. 20 million Lats. It must be emphasized that the amount of recovered funds is and will continue to be the only objective measure of Parex banka’s activity. We are sure that the improvement of the economic situation and our continuous purposeful work will lead us to the achieving good results.

In the first six months of this year we continued to revaluate all of the Bank's administrative costs consistently and responsibly. The thoroughly performed work and the balanced planning has yielded good results – administrative costs during the accounting period made up only 0.9% of the Bank’s average net value. This indicator once again speaks volumes about Parex banka’s administrative structure and its control efficiency considering that the Bank manages assets worth approximately 600 million Lats and services more than 5’000 clients on an everyday basis.

After the completed restructuring, retaining only the problematic assets with serious repayment problems, Parex banka has become a unique institution in the Baltic States. The aim determined for the Bank anticipates maximum recovery of the State invested funds invested within seven years. Therefore we are well aware that our task is not only to put all our efforts to completing it, but also to develop an open and honest communication with society. We gave such a pledge when we started working for the newly founded Parex Banka. Simultaneously we would like to ask the society to be understanding and tolerant in cases when detailed disclosure of certain information can have an adverse impact on the Bank, and this also means the tax payers’, interests. Conversely, the degree of detailed elaboration of the thoroughly prepared statement for the first six months of 2011 complies with all standards and requirements attaching to Parex banka, and it reflects the Bank’s ability to consistently perform the goals and tasks set forth in the restructuring plan.

Other significant events

On 17 May 2011 the Cabinet of Ministers supported the Strategy for Selling Parex Banka which was developed by Nomura International plc, an international financial consultant. A decision was adopted that Parex banka must continue implementing the business strategy elaborated by the mentioned financial consultant with the purpose of maximum recovery of the State investment. In order to increase and maintain the value of assets overtaken by the Bank, the priority business directions of the latter will continue to be restructuring of problematic assets, recovery of debt and professional management and selling of overtaken real estate objects. It is not planned to offer Parex banka as a whole to investors within the near future.

Considering that the specifics of Parex banka's activity are related to the recovery of significant funds, Parex banka has launched several serious proceedings during the accounting period. Among the initiated proceedings, the claim toward the Bank's previous Members of the Board and shareholders Valērijs Kargins and Viktors Krasovickis is of special importance. The aim of the claim is to receive compensation for losses caused to the Bank in the amount of at least 62 million Lats.

Most significant events after the accounting period

The agenda of Parex banka's Extraordinary Shareholder Meeting announced for 26 August 2011 includes a question on the increase of the Bank's core capital for the amount of 20 million Lats by emitting 20 million regular registered shares with voting rights, the nominal value of one share being one Lat.

The increase of the core capital is planned in accordance with the restructuring plan and it will ensure stability of Parex banka's activity and performance of regulatory requirements. Since capitalization of the existing investment made by the State is going to form the basis of transactions, additional State funding will not be necessary since, similarly to 2010, it is anticipated to use a part of the accrued interest for the State investment disposed with the Bank.

Christopher Gwilliam, Chairman of the Board

Solvita Deglava, Member of the Board

Jurijs Adamovičs, Member of the Board

Riga, 25 August 2011

Management of the Bank

Council of the Bank

Name	Position
Michael Joseph Bourke	Chairman of the Council
Sarmīte Jumīte	Deputy Chairman of the Council
Vladimirs Loginovs	Member of the Council
Mary Ellen Collins	Member of the Council

Management of the bank

Name	Position
Christopher John Gwilliam	Chairman of the Management Board, p.p.
Solvita Deglava	Member of the Management Board, p.p.
Jurijs Adamovičs	Member of the Management Board

Statement of Responsibility of the Management

The Management of AS Parex banka is responsible for the preparation of the unaudited financial information for the 1st half of 2011 of the Bank and the Group.

The unaudited financial information for the 1st half of 2011 is prepared in accordance with the source documents and present fairly the financial position of the Bank and the Group as at 30 June 2011 and the results of their operations, changes in shareholders' equity and cash flows for the six month periods ended 30 June 2011.

The unaudited financial information for the 1st half of 2011 is prepared in accordance with requirements of the Law on Financial Instruments Market and the Financial and Capital Market Commission's regulations No. 145 ”Regulations on Preparation of Public Quarterly Reports of Credit Institutions”.

Appropriate accounting policies have been applied on a consistent basis. Prudent and reasonable judgments and estimates have been made by the Management in the preparation of the report.

The Management of AS Parex banka are responsible for the maintenance of proper accounting records, the safeguarding of the Group's assets and the prevention and detection of fraud and other irregularities in the Group. They are also responsible for operating the Bank in compliance with the Law on Credit Institutions, regulations of the Financial and Capital Market Commission and other legislation of the Republic of Latvia applicable for credit institutions.

Balance Sheets as at 30 June 2011 and 31 December 2010

EUR 000's

	Reporting period *Unaudited* Group	Preceding reporting year *Audited** Group	Reporting period *Unaudited* Bank	Preceding reporting year *Audited** Bank
Cash and deposits with central banks	7	38 338	7	38 338
Balances due from credit institutions	28 137	96 310	27 898	93 678
Financial assets held for trading	3 293	1 776	3 293	1 776
Financial assets designated at fair value through profit and loss	0	0	0	0
Available-for-sale financial assets	3 705	84 533	15 871	84 533
Loans and receivables to customers	674 645	770 556	707 529	805 744
Held-to-maturity investments	34 478	34 445	34 478	58 857
Change in fair value of interest risk hedged portfolio	0	0	0	0
Prepayments and accrued income	2 205	5 488	2 181	5 485
Fixed assets	474	2 499	471	2 496
Investment property	44 919	28 187	24 835	19 389
Intangible assets	216	216	216	216
Investments in subsidiaries	0	0	85	85
Income tax assets	0	0	0	0
Other assets	53 966	64 689	11 896	12 449
Total assets	**846 045**	**1 127 037**	**828 760**	**1 123 046**

Due to central banks	0	0	0	0
Demand liabilities to credit institutions	17	0	17	0
Financial liabilities held for trading	75	2 849	75	2 849
Financial liabilities designated at fair value through profit and loss	0	0	0	0
Financial liabilities measured at amortised cost	791 736	1 035 153	791 736	1 035 168
Liabilities due to transfer of financial assets	0	0	0	0
Change in fair value of interest risk hedged portfolio	0	0	0	0
Accrued expenses and deferred income	1 753	2 591	1 715	2 553
Accruals	0	0	0	0
Income tax liabilities	0	0	0	0
Other liabilities	19 805	33 922	16 717	29 404
Total liabilities	**813 386**	**1 074 515**	**810 260**	**1 069 974**
Shareholders' equity	32 659	52 522	18 500	53 072
Total liabilities and shareholders' equity	**846 045**	**1 127 037**	**828 760**	**1 123 046**

Memorandum items				
Contingent liabilities	1 259	1 259	4 819	3 725
Financial commitments	223	282	27 954	28 263

* Auditors: SIA „PricewaterhouseCoopers”

Statements of Income

For the 6 months period ended 30 June 2011 and 30 June 2010

EUR 000's

	Reporting period *Unaudited*	Respective period of the preceding reporting year *Unaudited**	Reporting period *Unaudited*	Respective period of the preceding reporting year *Unaudited**
	Group	**Group**	**Bank**	**Bank**
Interest income	10 645	72 998	10 266	65 041
Interest expense	(25 339)	(83 158)	(25 336)	(79 487)
Dividends received	0	6	0	1 935
Commission and fee income	276	18 901	3	13 914
Commission and fee expense	(132)	(5 538)	(74)	(4 276)
Net gain/ (loss) on financial assets measured at amortised cost	0	179	0	0
Net gain/ (loss) on available for sale financial assets and financial liabilities	(5 507)	(720)	(5 507)	(1 726)
Net gain/ (loss) on held for trading financial assets and financial liabilities	0	(1 323)	0	(1 086)
Net gain/ (loss) on financial assets or financial liabilities designated at fair value though profit and loss	302	60	(131)	0
Change in fair value in hedge accounting	0	0	0	0
Gain/ (loss) from foreign exchange trading and revaluation of open positions	0	3 499	0	2 271
Profit/(loss) due to discontinued recognition of property, plant, equipment, investment properties or intangible assets	0	(1 851)	0	0
Other income	1 699	20 823	791	17 922
Other expense	(2 493)	(874)	(1 491)	(182)
Administrative expense	(8 090)	(42 885)	(4 931)	(31 154)
Amortisation and depreciation charge	(282)	(6 864)	(183)	(2 970)
Impairment charge and reversals, net	2 107	(77 117)	(14 929)	(68 057)
Impairment losses	0	0	0	0
(Loss)/ profit for the reporting period	**(26 814)**	**(103 864)**	**(41 522)**	**(87 855)**

Statements of Comprehensive Income:
EUR 000's

	01.01.2011.- 30.06.2011. *Unaudited*	**01.01.2010.- 30.06.2010.** *Unaudited**	**01.01.2011.- 30.06.2011.** *Unaudited*	**01.01.2010.- 30.06.2010.** *Unaudited**
	Group	**Group**	**Bank**	**Bank**
Net change in fair value revaluation reserve of securities	6 951	3 721	6 951	4 251
Other comprehensive income / (loss) for the period	6 951	**3 721**	**6 951**	**4 251**

Total comprehensive income / (loss) for the period	**(19 863)**	**(100 143)**	**(34 571)**	**(83 604)**

* Before the transfer of undertaking

Changes in the Group’s equity are as follows:

EUR 000’s

	Issued share capital	Share premium	Fair value revaluation reserve	Retained earnings	Total equity
Balance as at 31 December 2009*	**327 299**	**18 062**	**(17 527)**	**(130 126)**	**197 708**
Issue of new shares	44 820				44 820
Net loss for the period				(103 864)	(103 864)
Other comprehensive income for the period			3 721		3 721
Balance as at 30 June 2010*	**372 119**	**18 062**	**(13 806)**	**(233 990)**	**142 385**
Issue of new shares	13 802				13 802
Net loss for the period				(110 805)	(110 805)
Other comprehensive income for the period			7 140		7 140
Balance as at 31 December 2010	**385 921**	**18 062**	**(6 666)**	**(344 795)**	**52 522**
Issue of new shares					0
Net loss for the period				(26 814)	**(26 814)**
Other comprehensive income for the period			6 951		**6 951**
Balance as at 30 June 2011	**385 921**	**18 062**	**285**	**(371 609)**	**32 659**

Changes in the Bank’s equity are as follows:

EUR 000’s

	Issued share capital	Share premium	Fair value revaluation reserve	Retained earnings	Total equity
Balance as at 31 December 2009*	**327 299**	**18 062**	**(17 045)**	**(111 088)**	**217 228**
Issue of new shares	44 820				44 820
Net loss for the period				(87 855)	(87 855)
Other comprehensive income for the period			4 252		4 252
Balance as at 30 June 2010*	**372 119**	**18 062**	**(12 793)**	**(198 943)**	**178 445**
Issue of new shares	13 802				13 802
Net loss for the period				(145 302)	(145 302)
Other comprehensive income for the period			6 127		6 127
Balance as at 31 December 2010	**385 921**	**18 062**	**(6 666)**	**(344 245)**	**53 072**
Issue of new shares					0
Net loss for the period				(41 522)	**(41 522)**
Other comprehensive income for the period			6 951		**6 951**
Balance as at 30 June 2011	**385 921**	**18 062**	**285**	**(385 768)**	**18 500**

* Before the transfer of undertaking

Statements of Cashflows

For the 6 months period ended 30 June 2011 and June 2010

EUR 000's

	Reporting period *Unaudited*	Respective period of the preceding reporting year *Unaudited**	Reporting period *Unaudited*	Respective period of the preceding reporting year *Unaudited**
	Group	**Group**	**Bank**	**Bank**
Cash flows from operating activities				
Profit/ (loss) before tax	(25 385)	(116 200)	(41 371)	(101 387)
Amortisation of intangible assets, depreciation of fixed assets	282	6 864	184	2 970
Change in impairment allowances and other provisions	15 660	77 117	28 566	68 057
Other non-cash items	(3 409)	973	(1 255)	1 087
Cash generated before changes in assets and liabilities	**(12 852)**	**(31 246)**	**(13 876)**	**(29 273)**
Change in derivative financial instruments	(5 544)	1 191	(5 544)	1 176
(Increase) in other assets	2 652	(3 477)	3 593	(7 804)
(Decrease)/ increase in other liabilities	(4 812)	8 627	(3 367)	13 472
(Increase)/ decrease in trading investments	1 168	2 988	1 168	2 476
Decrease / (increase) in balances due from credit institutions	0	1 806	0	183 996
Decrease/ (increase) in loans and receivables from customers	73 804	49 361	71 223	36 487
(Decrease) in balances due to credit institutions	3 038	(200 979)	3 052	(214 583)
(Decrease)/ increase in deposits from customers	390	372 210	390	339 289
Cash generated from/ (used in) operating activities before corporate income tax	**57 844**	**200 481**	**56 639**	**325 236**
Corporate income tax paid	(1 429)	(284)	(151)	0
Net cash flow generated from/ (used in) operating activities	**56 415**	**200 197**	**56 488**	**325 236**
Cash flows from investing activities				
(Purchase) of intangible and fixed assets, net	(55)	713	(54)	763
Acquisitions and investments in subsidiaries	0	0	0	(13 075)
(Purchase)/sale of available-for-sale securities, net	87 666	0	89 985	0
Sale/ (purchase) of equity investments and other non-trading investments	0	39 889	0	63 056
Net cash flow generated from/ (used in) investing activities	**87 611**	**40 602**	**89 931**	**50 744**
Cash flows from financing activities				
Repayment of syndicated loans	(240 528)	(310 000)	(240 528)	(310 000)
Net cash flow used in financing activities	**(240 528)**	**(310 000)**	**(240 528)**	**(310 000)**
Net decrease in cash and cash equivalents for the period	**(96 502)**	**(69 201)**	**(94 109)**	**65 980**
Cash and cash equivalents at the beginning of the year	**123 322**	**533 258**	**120 689**	**470 784**
Cash and cash equivalents at the end of the period	**26 820**	**464 057**	**26 580**	**536 764**

* Before the transfer of undertaking

Consolidation Group as at 30 June 2011

No.	Name of company	Registration number	Registration address	Country of domicile	Company type*	% of total paid-in share capital	% of total voting rights	Basis for inclusion in the group**
1	AS “Parex banka"	LV-40003074590	Latvia, Riga LV-1010, Republikas laukums 2A	LV	BNK	100	100	MAS
2	Regalite Holdings Limited	CY-HE93438	Cyprus, Nicosia 1075, 58 Arch. Makarios 3 Avenue, Iris Tower, 6th floor, office 602	CY	PLS	100	100	MS
3	OOO "Parex Leasing and Factoring"	AZ-1105-T10-3749	Azerbaijan, Baku AZ1065, Dz.Dzabbarli 44, "Caspian Plaza"	AZ	LIZ	100	100	MS
4	OOO "Ekspress Lizing"	RU-1037867006726	Russia, St. Petersburg 192019, Sedova 11, liter A	RU	LIZ	100	100	MS
5	OOO "Laska Lizing"	UA-33104543	Ukraine, Kiev 03150, Dimitrova 5	UA	LIZ	100	100	MS
6	OOO "Parex Leasing"	RU-1047796715603	Russia, Moscow 111116, Energeticheskaja 3	RU	LIZ	100	100	MS
7	OOO "Extroleasing"	RU-1027739537220	Russia, Moscow 111116, Energeticheskaja 3	RU	LIZ	100	100	MS
8	SIA "Parex Private Banking"	LV-40003103438	Latvia, Riga LV-1050, Smilšu 7	LV	PLS	100	100	MS
9	OOO "Extrocredit"	RU-1067746758518	Russia, Moscow 111116, Energeticheskaja 3	RU	CFI	99	99	MMS
10	OOO "Parex Leasing and Factoring"	GE-205224461	Georgia, Tbilisi, Kazbegi avenue 44	GE	LIZ	100	100	MS
11	SIA "NIF"	LV-40103250571	Latvia, Riga LV-1010, Republikas laukums 2A	LV	PLS	100	100	MS
12	SIA “NIF Dzīvojamie īpašumi”	LV-40103253915	Latvia, Riga LV-1010, Republikas laukums 2A	LV	PLS	100	100	MMS
13	SIA “NIF Komercīpašumi”	LV-40103254003	Latvia, Riga LV-1010, Republikas laukums 2A	LV	PLS	100	100	MMS
14	SIA “NIF Zemes īpašumi”	LV-40103255348	Latvia, Riga LV-1010, Republikas laukums 2A	LV	PLS	100	100	MMS
15	UAB “NIF Lietuva”	LT-302462108	Lithuania, Vilnius LT03107, K.Kalinausko 13	LT	PLS	100	100	MMS
16	OÜ “Restruktureeritud Kinnisvarafond”	EE-11788043	Estonia, Tallinn 10119, Roosikrantsi 2	EE	PLS	100	100	MMS
17	SIA “NIF Projekts 1”	LV-50103300111	Latvia, Riga LV-1010, Republikas laukums 2A	LV	PLS	100	100	MMS
18	SIA “NIF Projekts 2”	LV-40103353475	Latvia, Riga LV-1010, Republikas laukums 2A	LV	PLS	100	100	MMS
19	SIA “NIF Projekts 3”	LV-40103353511	Latvia, Riga LV-1010, Republikas laukums 2A	LV	PLS	100	100	MMS

No.	Name of company	Registration number	Registration address	Country of domicile	Company type*	% of total paid-in share capital	% of total voting rights	Basis for inclusion in the group**
20	SIA “NIF Projekts 4”	LV-40103398418	Latvia, Riga LV-1010, Republikas laukums 2A	LV	PLS	100	100	MMS
21	SIA “NIF Projekts 5”	LV-40103398850	Latvia, Riga LV-1010, Republikas laukums 2A	LV	PLS	100	100	MMS
22	SIA “NIF Projekts 6”	LV-40103398865	Latvia, Riga LV-1010, Republikas laukums 2A	LV	PLS	100	100	MMS

*BNK – bank, CFI – other financial institution, LIZ – leasing company, PLS – company providing various support services.
** MS – subsidiary company, MMS – subsidiary of the subsidiary company, MAS – parent company.

Notes

Information about Parex banka's structure

As at 30 June 2011 the Bank had 2 foreign branches and 4 representative offices.

Issued share capital as at 30 June 2011

Shareholders	Nominal value (LVL)	Number of shares	Paid-in share capital (EUR)	Voting rights	Paid-in share capital (%)
SJSC "Privatizācijas Aģentūra"	1	221 933 292	315 782 625	156 283 292	81.83%
EBRD	1	39 631 824	56 391 005	39 631 824	14.61%
Other	1	9 662 179	13 748 042	5 468 323	3.56%
Total		**271 227 295**	**385 921 672**	**201 383 439**	**100%**

Information on certain parties that were related to the bank at the moment it received state aid

Pursuant to FCMC regulations on preparation of quarterly public reports of banks (Article 14[1]) the following table represents summary of material transactions with certain parties that were related to the Bank at the moment it received the State Aid:

EUR 000's

	1st half of 2011			1st half of 2010*		
	Period-end balance	**Average interest rate ****	**Interest income/ (expense)**	**Period-end balance**	**Average interest rate ****	**Interest income/ (expense)**
Loans issued by the Bank	2 641	0.00%	-	44 815	2.14%	457
Deposits placed with the Bank	-	-	-	39 842	1.53%	(1 387)
Subordinated financing provided to the bank	51 230	3.99%	(1 538)	51 232	6.73%	(2 701)

* Before the transfer of undertaking

** According to period-end rates

Subordinated financing contracts were entered into force in 2008 and have maturities ranging 2015 through 2018. Subordinated financing is LVL and EUR denominated. Prior repayment can be unilaterally requested only upon liquidation of the Bank.

The following table represents the details of Group's subordinated capital:

EUR 000's

Counterparty	Residence country	Currency	Issue size, 000's	Interest rate	Original agreement date	Original maturity date	Amortised cost (EUR 000's) 30/06/2011	Amortised cost (EUR 000's) 31/12/2010
Notes-private placement	UK	EUR	20,000	6.078%	28/12/2007	28/12/2017	18 823	18 788
Private person	Latvia	LVL	7,500	6M Rigibid + 3%	28/09/2007	26/09/2017	10 673	10 674
Private person	Latvia	LVL	7,500	6M Rigibid + 3%	28/09/2007	26/09/2017	10 673	10 674
Notes – public issue	n/a	EUR	5,050	11%	08/05/2008	08/05/2018	5 435	5 435
Private person	Latvia	EUR	15,000	12%	20/06/2008	14/05/2015	15 085	15 085
Private person	Latvia	LVL	1,500	6M Rigibid + 3%	30/10/2008	30/10/2018	2 134	2 134
Private person	Latvia	LVL	1,500	6M Rigibid + 3%	30/10/2008	30/10/2018	2 134	2 134
Private person	Latvia	LVL	2,284	6M Rigibid + 3%	04/12/2008	18/09/2015	3 250	3 250
Private person	Latvia	LVL	2,284	6M Rigibid + 3%	04/12/2008	18/09/2015	3 250	3 250
Private person	Latvia	LVL	1,416	6M Rigibid + 3%	04/12/2008	29/09/2015	2 015	2 015
Private person	Latvia	LVL	1,416	6M Rigibid + 3%	04/12/2008	29/09/2015	2 015	2 015
Total							**75 488**	**75 455**

Financial instruments as at 30 June 2011 and 31 December 2010

EUR 000's

	Reporting period *Unaudited*	Preceding reporting year *Audited**	Reporting period *Unaudited*	Preceding reporting year *Audited**
	Group	Group	Bank	Bank
Financial assets held for trading (net):	**3 298**	**1 776**	**3 293**	**1 776**
Available-for-sale financial assets (net):	**3 705**	**84 533**	**15 871**	**84 533**
Russia (gross)	-	-	*30 804*	-
Impairment allowance	-	-	*(18 527)*	-
Russia (net)	112	21 026	12 277	21 026
Germany	-	23 544	-	23 544
Great Britain	-	13 398	-	13 398
Republic of Kazakhstan	-	14 287	-	14 287
Other	-	8 766	-	8 766
Latvia	3 593	3 512	3 594	3 512
Held-to-maturity investments (net):**	**34 478**	**34 445**	**34 478**	**58 857**
Russia (gross)	-	-	-	*33 196*
Impairment allowance	-	-	-	*(8 783)*
Russia (net)	-	-	-	24 412
Latvia	34 478	34 445	34 478	34 445
Total	**41 481**	**120 753**	**53 641**	**145 166**

* Auditors: SIA „PricewaterhouseCoopers”

**The fair value of held-to-maturity investments as at 30 June 2011 was 28 820 (51 828) *EUR 000's* for the bank and 28 820 (27 414) *EUR 000's* for the group.

Financial liabilities measured at amortised cost as at 30 June 2011 and 31 December 2010

EUR 000's

	Reporting period *Unaudited*	Preceding reporting year Audited*	*Reporting period* *Unaudited*	Preceding reporting year Audited*
	Group	Group	*Bank*	Bank
Loans from credit institutions	11 678	254 146	11 678	254 146
Deposits from customers	704 570	705 552	704 570	705 567
Subordinated liabilities	75 488	75 455	75 488	75 455
Total	**791 736**	**1 035 153**	**791 736**	**1 035 168**

* Auditors: SIA „PricewaterhouseCoopers”

Risk Management

The Group’s risk is managed according to principles set out in Group’s Risk and Capital Management Policy. The Group adheres to the following key risk management principles:

- Undertaking an acceptable risk level is one of the Group’s main functions in all areas of operation. Risks are always assessed in relation to the expected return. Risk exposures that are not acceptable for the Group are, where possible, avoided, limited or hedged;
- The Group does not assume new high or uncontrollable risks irrespective of the return they provide. Risks should be diversified and those risks that are quantifiable should be limited or hedged;
- Risk management is based on awareness of each and every Group’s employee about the nature of transactions he/she carries out and related risks;
- Risk limit system and strict controls are essential elements of risk management. Control of risk level and compliance with limits is ensured by structured risk limit systems for all material risks;
- The Group aims to ensure as low as possible risk exposure and low level of operational risk.

Risk management is an essential element of the Group’s management process. Risk management within the Group is controlled by an independent unit unrelated to customer servicing - Risk Management Division.

The Group is exposed to the following main risks: credit risk, market risk, interest rate risk, liquidity risk, currency risk and operational risk. The Group has approved risk management policies for each of these risks, which are briefly summarised below.

Credit risk

Credit risk is the risk that the Group will incur losses from debtor’s non-performance or default. The group is exposed to credit risk in to its lending, investing and trading activities, as well as in respect to the guarantees issued to third parties and other off-balance sheet commitments to third parties.

Credit risk management is based on adequate risk assessment and decision-making. For material risks, risk analysis is conducted by independent Risk Management Division. The analysis of credit risk comprises evaluation of customer’s creditworthiness and collateral and its liquidity. The analysis of creditworthiness of a legal entity includes analysis of the industry, the company, and its current and forecasted financial position. The analysis of creditworthiness of an individual includes the analysis of the customer’s credit history, income and debt-to-income ratio analysis, as well as the analysis of social and demographic factors. In the event of material risks, lending decision is made by the Credit Committee, and further reviewed by the Bank’s Management Board.

The Group reviews its loan portfolio on a regular basis to assess its quality and concentrations, as well as to evaluate the portfolio trends.

Credit risk identification, monitoring and reporting is the responsibility of Risk Management Division.

Market risk

Market risk is the risk that the Group will incur a loss as a result of the mark-to-market revaluation of balance sheet and off-balance sheet items caused by changes in market values of financial instruments due to changes in foreign exchange rates, interest rates and other factors.

Due to the specific nature and limited scale of the Bank's operations since the split of the bank on August 1, the Group does not take up new market risks. Market risk assessment, evaluation of undertaken positions, as well as risk monitoring and reporting is carried out by Finance Planning and Control Division and Risk Management Division.

Interest rate risk

Interest rate risk is related to the negative impact of interest rate changes on the Group's interest income and economic value.

Interest rate risk measurement, management and reporting in the Group is coordinated by Finance Planning and Control Division and Risk Management Division. After the split of the Bank on 1 August 2010 due to the specifics of Bank's operations it has only limited means to manage its interest rate risk. Bank's interest rate risk assessment and relevant decision making is carried out by the Bank's Management Board.

Liquidity risk

Liquidity risk is the risk that the Group will be unable to meet its legal payment obligations. The purpose of liquidity risk management is to ensure the availability of liquid assets sufficient to meet potential obligations.

Under ordinary circumstances the Group manages its liquidity risk in accordance with the Group's Liquidity Risk Management Policy. Liquidity risk is assessed and related decisions are made by the Bank's Management Board. Daily liquidity management, as well as liquidity risk measurement, monitoring and reporting, is ensured by the Risk Management Division and Finance Planning and Control Division. Liquidity risk management in the Group is coordinated by the Risk Management Division and Finance Planning and Control Division. However the main source of liquidity is the funding provided by the Ministry of Finance. In 2011 the Bank was in compliance with liquidity ratio requirements.

Currency risk

Currency risk is related to mismatch in foreign currency asset and liability positions that impact the Group's cash flow and financial results via fluctuations in currency exchange rates.

Currency risk management in the Group is carried out in accordance with the Group's Currency Risk Management Policy. Day-to-day currency risk monitoring, management and reporting is the responsibility Risk Management Division and Finance Planning and Control Division. The Group has set a limit for open currency positions in each currency at 10% of its equity, and the limit for the total open currency position at 20% of its equity. The limits are in compliance with the requirements of Latvian legislation.

Operational risk

Operational risk is the risk of suffering losses resulting from processes that are deficient or non-compliant with requirements of external and internal regulations, losses resulting from actions of employees and system malfunctioning, as well as losses resulting from actions of third parties or from other external conditions, including legal risk (risk of penalty fees, sanctions applied by external institutions, losses resulting from litigation and other similar events), but excluding strategic risk and reputation risk. The Group further divides operational risk into the following categories: personnel risk, process risk, IT and systems risk, external risk.

The Group does not undertake / accept operational risks with potential impact exceeding 10% of the Group's net annual revenues, or risks with unquantifiable impact that are concurrently unmanageable (it is impossible to prevent such risks or provide for their consequences – e.g. non-compliance with legal regulations etc.), irrespective of the financial gains this could bring (i.e., the Group does not perform business activities incurring such operational risks).

The Group applies following approaches for operational risk management:

- Defining operational risk indicators – use of statistical, financial and other indicators that reflect the level of various operational risk types and its changes within the Group;
- Operational risk measurement by recording and analysing operational risk events, the extent of the respective damage incurred, causes and other related information (data base of operational risk losses and incidents);
- "Four-eye-principle" and segregation of duties;
- Business continuity planning;
- Insurance;
- Investments in appropriate data processing and information protection technologies.