AS Reģionālā investīciju banka

Consolidated and Bank's annual report for the year ended 31 December 2019

Prepared in accordance with International Financial Reporting Standards as adopted in the European Union

04.03.2020

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Management report

In 2019, AS Reģionālā investīciju banka (hereinafter – the Bank) developed successfully in accordance with the previously approved strategy. One of the main factors promoting development in 2019 was the active transformation of the Bank's business model, shifting the Bank's business from the non-residential segment to a new business niche – providing banking services to Latvian and EU small and medium enterprises (SME) focusing on the Bank's basic product – SME lending. In the reporting period net profit of the Bank amounted to EUR 2.99 million exceeding the budgeted results of the year 2019 by 39%. Return on equity (ROE) and return on assets (ROA), based on the results of the year, amounted to 8.67% and 1.15% respectively.

At the beginning of 2019, the Financial and Capital Market Commission (FCMC) set the capital adequacy requirement for the Group at 11.9%. The Bank continued to exceed this requirement, and as at 31 December 2019 the Bank's ratio was 26,95%, which included the preservation of capital reserve of 2.5%. The Bank constantly maintained its liquidity ratio to comply with the minimum requirement set by the FCMC at the rate of 40%, and as at 31 December 2019, the Bank's liquidity ratio amounted to 86.90%.

Overall economic situation

2019 was the tenth consecutive year that Latvian economy had continued to grow; however, as a result of the slowdown of global economic development the Latvian GDP growth rate also fell. Overall, in the first three quarters of 2019, Latvian economy grew by 2.5%. In 2019, the GDP growth was slower than in the previous year and the slowdown was mostly caused by the slower growth of investments and in the construction sector as well as the declining growth of global economy. In 2019, the economic growth indicators in Latvia were largely based on the effect of short-term activities. Pessimistic development expectations for the next year in a number of Latvian trade partners hinder faster rebound of external demand growth in 2020 in Latvia.

In the first three quarters of 2019, the economic development of Latvia was most facilitated by the growth in the following sectors: trade (+4.8%), agriculture and forestry (+11,5%) and professional services (+6.0%). Fall in external demand continued its negative impact on the performance of almost all main manufacturing sectors. The construction sector experienced growth slowdown (+3.8% in comparison with +20% in 2018), which had already been predicted given the decline in investments and maximum utilization of the EU funds. Internal demand plays an increasingly important role in GDP growth; however, in comparison with the previous year the increase in internal demand was more moderate as the decline in external demand had also a stronger impact on internal economic decisions. In 2018, investments grew by 15.8%, whereas in the first three quarters of 2019 – only by 5.1%.

In 2019, there was an overall stabilization of the key performance indicators of the Latvian banking sector. Due to the ongoing transformation of the banking sector, total deposits exhibited a decreased share of foreign deposits – from 53.4% in 2015 to 19.5% at the end of September 2019. The geographic breakdown of deposits revealed that 93% of all deposits were those by residents of Latvia and other EU countries. The overall trend in 2019 demonstrated an inability to show a sustainable growth in corporate lending. The credit institutions adhered to conservative lending policy and they were more critical concerning cooperation with potentially risky customers. In the first three quarters of 2019, the Latvian banking sector reported a profit of EUR 203.3 million, a 20% yoy decrease; however, at the end of September, the return on capital (ROE) reached 10.7% (7.0% the EU average). The capital and liquidity ratios remained at high levels ensuring sufficient reserves for covering potential losses.

Overall economic situation *(cont'd)*

According to the projections of the Bank of Latvia, GDP growth in 2019 and 2020 might be 2.3% and 2.6% respectively. The growth in domestic demand will be more moderate than the projected one and investment growth is expected to be especially slow. The projected inflation by the Bank of Latvia is to be 2.8% in 2019 and 2.4% – in 2020.

Operations during the reporting period

Within the framework of the Bank's Development Strategy, the year 2019 was a transitional year for the Bank between the previous 18-year history of its operations and the new business model initially defined in the Bank's Development Strategy 2018-2021, approved in spring 2018. Considering the new strategy implementation activities in the second half of 2018 and their results as well as the changes that took place in the Latvian banking sector in 2018 and the first quarter of 2019, the Bank reviewed its strategy and in April 2019 approved a new Development Strategy 2019-2022, substantially specifying a number of parameters, including the change in the positioning of the Bank in the market from a universal bank to a "niche" bank, specializing in lending. The main aim of the strategy is development of a sound and effective specialized European bank that offers professional advice and a range of products and services according to market demand in lending and corporate finance areas. The Bank's products are oriented to legal entities – Latvian/EU SMEs, as well as to private individuals – employees, managers and owners of the SMEs serviced by the Bank.

The year 2019 was devoted to achieving the targets set in the new strategy, namely, establishing a competent and experienced sales team focusing on domestic market, development of new lending products for local SMEs, obtaining respective approvals for such products from the regulator and marketing thereof as well as active work with the local potential customer base in the SME lending segment. Focus was also on achieving such targets as ensuring customer risk acceptable to the Bank, the development of ML/TF risk control system, optimization of administrative expenses and maintaining high development level in all business lines.

In 2019, the Bank, operating in its new market segment, applied a prudent lending policy while getting acquainted with the specifics of the local SME lending market and gaining experience in this area. As a result of such a prudent lending policy, in 2019 the Bank issued new loans of EUR 29.4 million, which constitutes a 41.3% increase compared to the year 2018 (EUR 17.25 million), whereas the loans repaid amounted to EUR 70.5 million (2018: EUR 36.45 million). Consequently, the total loan portfolio decreased by 36%. Notwithstanding such an overall portfolio dynamic, the Bank maximally maintained profitability of its basic product due to the increased annual effective interest rate – the interest income fell only by 10.2% and reached EUR 6.3 million. As at 31 December 2019, the total loan portfolio amounted to EUR 71,2 million. In the reporting year, ECL allowances decreased by 47%. In January 2019, the Bank started attracting deposits in cooperation with the German deposit broker Deposit Solutions. The aim of cooperation is to diversify the Bank's sources of financing, establish a stable depositor relationship and to focus on EU-resident market. At the end of 2019, through a deposit platform, the Bank had attracted deposits total EUR 34.8 million with various maturities. In 2019, the deposit broker Deposit Solutions proved itself as an effective and flexible solution for attracting EU depositors and the Bank intends to continue the cooperation with this partner in 2020, too.

Management report *(cont'd)*

Bank's activities during the reporting period *(cont'd)*

In 2019, meeting the requirements laid down in the revised AML/CTF Law and new ML/TF Risk Management Strategy, the Bank considerably reduced its non-resident customer base – overall 1,054 customer accounts were closed in 2019. The number of shell companies was reduced to the absolute minimum; at the end of 2019 there were only 178 such customers. As a result of customer risk mitigation measures, at the end of 2019 the average customer risk level of the Bank was reduced from 'high' to 'medium'.

On 15 April 2019, the following changes in the composition of the Management Board took place - Alda Odiņa took the position of a Board Member in charge of AML/CTF and Dace Gaigala became a Board Member. In June 2019, Gints Gritans resigned from the position of a Board Member while continuing to perform the functions of the CFO and Head of the Finance and Resource Department of the Bank. In January 2019, the position of a Business Development Officer was established and the Bank's internal structure was also reviewed and optimized. These changes were mainly aimed at strengthening the structural units responsible for the development of the Bank's business lines, incl. establishing the Corporate Banking Department, specializing in the provision of banking services to Latvian SMEs and active sales of the Bank's lending products.

Profit distribution as suggested by the management Board

The management Board suggests that the profit for the reporting year should be transferred to retained earnings.

Future plans and prospects

In 2020, the management of the Bank plans to proceed with active implementation of its strategy approved in the previous year maintaining a niche bank's focus on providing lending and other banking services to SME. The main strategic product of the Bank is corporate lending, which through cooperation process is supplemented by other products from the range of products and services provided by the Bank. The customer attracting and lending activities carried out in 2019 as well as inputs in the domestic market confirm that the strategic direction chosen by the Bank has a clear perspective for the Bank to continue as a going concern.

The sound financial position of the Bank enables in 2020 the management to plan more active involvement in attracting target customers and increasing resources and competences for the development of the database, if necessary. Achieving the objectives set by the Bank will be facilitated by targeted marketing and sales promotion activities. Attraction of new customers and increase of lending in the target segments are among the key priorities of the Bank's management in 2020. Within the framework of the Bank's Marketing and Communications Strategy, in 2020 the Bank will also focus on developing its image in the local market alongside with targeted measures for supporting the sales team in attracting new customers and lending projects.

In 2020, the Bank plans to proceed with the development of its product line and adaptation to its strategic goals, focusing on improving and maintaining its loan portfolio. Reducing the range of products in the business lines that are not the Bank's priority is considered. Within the framework of the new IT Strategy, fully aligned to the Bank's strategy approved in April 2019, the Bank intends working on developing a new Internet bank solution in 2020 and its implementation in the next three years. For the Bank, this is a significant decision which after its realization in full will allow to significantly improve the service quality and the Bank's image in the local business community.

Future plans and prospects (cont'd)

As a result of the administrative expense optimization measures taken in 2018 and 2019, the Bank has reached the optimal number of employees and amount of related expenses. One of the 2020 objectives within this process is improving the staff competences and professional skills.

The Bank's profit forecast for 2020 is adequately conservative. The budget for 2020 foresees that the Bank will close the year 2020 with a net profit of EUR 1,13 million. Moreover, the expenditure part of the budget includes investments in the IT system development, finalizing several technological development projects started in 2018-2019.

Aleksandrs Jakovļevs
Chairman of the Board

Yuriy Rodin
Chairman of the Council

Riga, 04 March 2020

The Supervisory Council and the management Board of the bank

As at 31 December 2019 and at the date of signing the financial statements

Supervisory Council

		Date of appointment
Yuriy Rodin	Chairman of the Council	Re-elected – 15.05.2017
Mark Bekker	Deputy Chairman of the Council	Re-elected – 15.05.2017
Dmitrij Bekker	Member of the Council	Re-elected – 15.05.2017
Alla Vanetsyants	Member of the Council	Re-elected – 15.05.2017
Irina Buts	Member of the Council	Re-elected – 15.05.2017

Management Board

		Date of appointment
Aleksandrs Jakovlevs	Chairman of the Board	Re-elected - 05.08.2019
Andrejs Gomza	Member of the Board	30.11.2016
Alda Odiņa	Member of the Board	15.04.2019
Dace Gaigala	Member of the Board	15.04.2019
Vita Matvejeva	Member of the Board	06.02.2020

During 2019, the following changes took place in the composition of the management Board of AS Reģionālā investīciju banka on 15 April 2019 Alda Odiņa and Dace Gaigala were appointed Members of the Board and Gints Gritans was dismissed on 5 June 2019. On 6 February 2020, another new board member, Vita Matvejeva, joined the Board.

Aleksandrs Jakovlevs
Chairman of the Board

Yuriy Rodin
Chairman of the Council

Riga, 04 March 2020

Statement of management Responsibility

The Supervisory Council and the Board of Directors (hereinafter - the management) of the Bank are responsible for the preparation of the Consolidated financial statements of the Bank and its subsidiary (hereinafter – the Group) and the Bank's financial statements.

The Consolidated and Bank's financial statements on pages 17 through 102 are prepared in accordance with the source documents and present fairly the financial position of the Group and the Bank as at 31 December 2019 and the results of their operations and cash flows for the reporting year 2019.

The financial statements are prepared in accordance with International Financial Reporting Standards as adopted in the European Union on a going concern basis. 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 financial statements.

The management of the Bank is responsible for the maintenance of proper accounting records, the safeguarding of the Bank's assets and the prevention and detection of fraud and other irregularities in the Bank. 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 Bank of Latvia and other legislation of the Republic of Latvia applicable for credit institutions.

Aleksandrs Jakovlevs
Chairman of the Board

Yuriy Rodin
Chairman of the Council

Riga, 04 March 2020

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Translation from Latvian

INDEPENDENT AUDITORS' REPORT

To the Shareholders of Reģionālā Investīciju Banka AS

Report on the Audit of the Financial Statements

Opinion

We have audited the accompanying consolidated financial statements of Reģionālā Investīciju Banka AS and its subsidiary (the Group) and the accompanying financial statements of Reģionālā Investīciju Banka AS (the Bank) set out on pages 17 to 102 of the accompanying Annual Report, which comprise the statements of financial position as at 31 December 2019, and the statements of comprehensive income, statements of changes in equity and statements of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies and other explanatory notes.

In our opinion, the accompanying financial statements of the Group and the Bank give a true and fair view of the financial position of the Group and the Bank as at 31 December 2019, and of financial performance of the Group and the Bank and cash flows of the Group and the Bank for the year then ended in accordance with the International Financial Reporting Standards (IFRS) as adopted by the European Union.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing adopted in the Republic of Latvia (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the International Code of Ethics for Professional Accountants (including International Independence Standards) (IESBA Code) together with the independence requirements included in the Law on Audit Services of Republic of Latvia that are relevant to our audit of the financial statements in the Republic of Latvia. We have fulfilled our other ethical responsibilities in accordance with the Law on Audit Services of Republic of Latvia and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Material Uncertainty Related to Going Concern

We draw attention to Note 37 of the consolidated and the Bank's separate financial statements, which indicates that in May 2018 amendments to the Law on the Prevention of Money Laundering and Terrorism Financing came into force prohibiting the service provision to a part of shell-companies. The Group and the Bank has revised the business model and started to implement a new development strategy. Given that the Group and the Bank are in the early stage of new business model implementation as defined in the development strategy, there is uncertainty on whether and how the Group and the Bank will succeed in implementing the new strategy. These events or conditions indicate that a material uncertainty exists that may cast significant doubt on the Group's and the Bank's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

Emphasis of matter

We draw attention to Note 37 of the consolidated and the Bank's separate financial statements, which indicates that in the third quarter of 2019, the Financial Capital and Market Commission (FCMC) performed an inspection at the Bank on the prevention of money laundering and terrorist and proliferation financing and the sanctions risk management. As of the date of signing these financial statements, the results of the FCMC inspection had not yet been received.

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Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the Group and the Bank of the current period. These matters were addressed in the context of our audit of the financial statements of the Group and the Bank as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the financial statements* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the financial statements of the Group and the Bank. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying financial statements of the Group and the Bank.

Key audit matter	How we addressed the key audit matter
Loan loss Impairment (the Consolidated and the Bank's separate financial statements)	
The carrying amount of loans to corporate and individual customers as at 31 December 2019 amounted to EUR 59 298 thousand in the Bank's separate financial statements and EUR 54 755 thousand in the Consolidated financial statements; the impairment reversal recognized amounted to EUR 1 117 thousand in the Bank's separate financial statements and EUR 1 144 thousand in the Consolidated financial statements in 2019. The total impairment loss allowance as at 31 December 2019 amounted to EUR 11 862 thousand in the Bank's separate financial statements and EUR 11 834 thousand in the Consolidated financial statements. Since 1 January 2018, the Group and the Bank has introduced the expected credit loss model under IFRS 9. The basis of the Bank's and the Group's impairment provision policy is presented in the accounting policies section in Notes 3(m) and 4(a) to the financial statements. Critical accounting estimates and judgments, disclosures of loans and guarantees and the credit risk management are set out in Notes 3(m), 4(a) and 13 to the financial statements. Loan receivables are significant to the total assets of the Consolidated and the Bank's separate financial statements. The Group and the Bank have significant exposures to the borrowers in foreign jurisdictions including those in the Ukraine. We identified this area to be significant for the audit because measurement and recognition of allowances for loan loss impairment reflected in the Group's and the Bank's expected credit loss model is associated with significant estimation as it requires the management to exercise judgement and apply complex and subjective assumptions both about the timing and amounts of such	Our audit procedures included, among others, the following: We gained understanding and tested the key controls over the loan issuance, booking and monitoring and loan impairment provisioning processes. We obtained and read the Group's and the Bank's Impairment provisioning policy that is based on IFRS 9 and involved our internal IFRS 9 specialists to assist us in the assessment of its compliance with the requirements of IFRS 9. In addition to testing the key controls, we selected a sample of loans with higher risk characteristics such as significant exposures arising from the related borrower groups, restructured loans or borrowers in foreign jurisdictions, exposures arising from delayed payments outstanding on the reporting date. The sample of loans was assessed as to the existence of significant increase in credit risk and default triggers by reviewing the underlying loan documentation and discussing the respective loans with the representatives of the Loan Department and the Debt Collection Department. As concerns non-performing loans, we reviewed the forecasts of future cash flows used in the assessment of loan impairment, evaluated the key assumptions made by the management such as the applied discount rates, collateral values (by involving our valuation specialists), forecasted business performance and, as applicable, cost to repossess the collateral, collateral sales costs and sales periods. The sample of loans was examined considering whether all impairment events identified by us had also been identified by the Group's and Bank's management. As to the performing loans and receivables, we assessed whether the borrowers exhibited the significant increase in credit risk or the possible default risk that may affect meeting their scheduled repayment obligations. We reviewed the Group's and the Bank's accounting policies and the management's assumptions relating to the estimation

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impairment. Key areas of judgement include the identification of exposures with a significant deterioration in credit quality, assumptions used in the expected credit loss model such as the financial condition of the counterparty, expected future cash flows and forward looking macroeconomic factors. Individual impairment allowances recognized by the Group and the Bank mostly relate to large, individually monitored exposures to corporates and individuals. Therefore, the assessment of the aforementioned exposures is based on the knowledge about each individual borrower and often on the estimated fair value of the relevant collaterals, the assessment of customers which are likely to default, and the future cash flows relating to loans. Due to the above circumstances, we considered loan impairment assessment to be the key audit matter.	of expected credit loss. For a sample of the loans we assessed the significant expected credit loss model components: staging, Loss Given Default (LGD), Probability of Default (PD), Exposure at Default and assessed whether the Group and the Bank has calculated estimated expected credit loss in line with the provisioning policy. We performed analytical procedures, such as a comparison of loan loss impairment allowance balances to industry levels, comparison to prior year, movements between stages etc. We also assessed the adequacy of the financial statement disclosures in Notes 3 (m), 4(a) and 13.
Anti-money Laundering (regulatory requirements regarding anti-money laundering) (the Consolidated and the Bank's separate financial statements)	
As disclosed in Note 37, in 2018, the amendments to the Law on the Prevention of Money Laundering and Terrorism and Proliferation Financing (AML/CFT) have come into force. The banks in Latvia were prohibited to establish and maintain the business relationship with shell-companies that possessed certain indications. As the Group and the Bank historically have cooperated with the shell-companies, these events required the Group and the Bank to revise their AML policies as well as the clients' base. In late 2018 the FCMC carried out the inspection to assess the fulfilment of the requirements specified in Law on AML/CFT concerning the prohibition to cooperate with shell companies and issued findings report. Additionally, during 2017 the Group and the Bank was involved in an administrative proceeding initiated by Latvian financial services regulator, the FCMC, concerning the failure to comply with anti-money laundering requirements embedded in Latvian legislation and on 26th June 2017 the FCMC announced a regulatory fine amounting to EUR 570 thousand imposed on the Bank. The Group and the Bank acknowledged misconduct and paid the imposed fine during 2017. The FCMC and the Bank concluded a mutual administrative agreement wherein the FCMC laid down requirements for the Bank with a view to strengthening its internal anti-money laundering control system so that it complies with the FCMC requirements which are considered a key requisite for the Group's and the Bank's successful operations in the future. As described in Note 37 of the consolidated and the Bank's separate financial statements, in the third quarter of 2019, the FCMC performed an inspection at the Bank	Our audit procedures included, among others, the following: We reviewed the Group's and the Bank's AML/CFT risk management strategy for 2019-2021 and discussed the implementation status. We discussed the matter with the Group's and the Bank's representatives responsible for compliance with anti-money laundering requirements, the improvement plan and its implementation. We reviewed and evaluated the Bank's action plan in relation to the FCMC findings and its implementation by inspecting the implementation status reports and correspondence on the implementation with the regulator. We gained understanding of Bank's internal policies and procedures and involved our internal AML specialists in the assessment of policy compliance with AML/CFT, Economic Sanctions (ES) laws and regulations. We gained understanding and tested the key controls over the Client Onboarding, Enhanced due diligence, Transaction monitoring and Sanctions screening processes and reviewed their compliance with AML/CFT, ES laws and regulations. We discussed with the Group's and the Bank's representatives the strategy of the clients' termination that the Group and the Bank pursued after the amendments to the Law on AML/CFT came into force. We tested a sample of terminated clients to evaluate whether the cooperation had been terminated. We reviewed communication with the FCMC in order to identify undisclosed or unrecorded violations noted by the regulatory institution.

on the prevention of money laundering and terrorist and proliferation financing and the sanctions risk management. At the date of signing these financial statements, the results of the FCMC inspection had not yet been received. Given the importance of the matter to the Group's and the Bank's reputational risk and significant impact on the future operations, we have this as a key audit matter.	We have evaluated our observations and findings resulting from our audit procedures performed and their impact on our auditors' report as well as communicated them together with our recommendations to the Group's and the Bank's management and audit committee. We also assessed the adequacy of the disclosures relating the matter in Note 4(i) and Note 37 to the financial statements.
Valuation of repossessed assets (the Consolidated and the Bank's separate financial statements)	
As disclosed in Note 19 to the financial statements the Group and the Bank have repossessed real estate as part of the loan recovery process and have accounted them both in the Consolidated and the Bank's separate financial statements as at 31 December 2019 amounting to EUR 13 312 thousand and EUR 3 327 thousand respectively. The largest repossessed property recorded in the Consolidated financial statements amounting to EUR 9 985 thousand is located in Germany (Berlin) and there are certain legal restrictions to be resolved. Some of the real estate is located in Ukraine (the Consolidated and the Bank's separate financial statements) and selling of the respective properties might require considerable time. Determining whether an impairment for any of the repossessed real estate should be recognized requires the Group's and the Bank's management to make significant assumptions and involves judgements. As a result of the Group's and the Bank's management impairment assessment, no impairment charge has been recognized in year 2019. Due to the above circumstances, we consider the impairment assessment of repossessed real estate to be a key audit matter.	Our audit procedures included, among others, the following: We obtained understanding about the management's approach to the accounting and assessment of the recoverable amounts applied to the respective repossessed assets. We assessed the ownership of the repossessed real estate by reviewing the respective country's land registry documents. We obtained and reviewed initial valuations and their updates of the repossessed real estate made by independent certified third party valuators. We assessed the independence and competence/ experience of the engaged third party valuators. We involved valuation specialists to assist us in reviewing the initial valuation reports and their updates on the selected largest repossessed real estate objects. Our valuation specialists reviewed and assessed the estimates and key assumptions used and methodologies applied to determine the recoverable amounts of the repossessed real estate. For the additional work done on the largest repossessed real estate located in Germany see the key audit matter "Recoverability of investment in and loan issued to the subsidiary Grunewald Residence Ltd". We assessed the classification and valuation of the assets according to IFRS. We also assessed whether the disclosures in Notes 3(p), 3(gg) and 19 to the financial statements comply with the IFRS requirements and considered whether the disclosures on the application of judgement in estimating the recoverable amount and the sensitivity of the results of those estimates reflect the risks associated with impairment of repossessed real estate.

Recoverability of investment in and loan issued to the subsidiary Grunewald Residence Ltd (the Bank's separate financial statements)	
In the Bank's separate financial statements as at 31 December 2019 the carrying amount of EUR 6 100 thousand of investment in the subsidiary, Grunewald Residence Ltd, was reported. The loan issued to the subsidiary amounted to EUR 4 570 thousand. The core business of the subsidiary is holding the repossessed asset located in Germany taken over in the year 2017. As described in Note 15, the ultimate goal of the Bank's management is successful sale of the respective asset (in a development stage) once legal restrictions related to the asset are resolved. In order to increase the value of the asset and also to strengthen the Grunewald Residence Ltd position in court, German architects have been contracted to develop the site project and obtain construction permits for the potential future development of the land when the legal restrictions are removed and the old buildings demolished. The determination of the recoverable amounts of the investment in the subsidiary and the loan to the subsidiary is a complex process and requires the management to make subjective judgements, including those in respect of resolution of the legal restrictions and also future operating cash flows, growth rates and discount rates related to the development of the repossessed asset. Due to the above circumstances, we consider recoverability of investment in the subsidiary and the loan issued to the subsidiary to be a key audit matter.	Our audit procedures included, among others, the following: We assessed the ownership of the subsidiary Grunewald Residence Ltd and land in Berlin, Germany, by obtaining the subsidiary incorporation documents and reviewing the Germany Land register documentation and the third-party purchase agreement of the land. We obtained and reviewed the initial valuation and its update of the repossessed real estate made by the independent certified third party valuator as a key evidence supporting recoverability of the investment in the subsidiary and related loan to the subsidiary. We assessed the independence and competence/ experience of the engaged third party valuator. We also reviewed and assessed the offers received by the lawyers and insolvency administrator to buy the land plot. The received offers also included financing plans confirmed by the banks. We involved valuation specialists to assist us in reviewing the updated valuation report. Our valuation specialists reviewed and assessed the estimates and key assumptions used and methodologies applied to determine the recoverable amount of the land plot. We reviewed the legal opinion on the potential outcome of the legal proceedings in respect of the restrictions and assessed how the management had incorporated this information in its projections on estimation of recoverability of the investment in the subsidiary and loan issued to the subsidiary. We discussed the facts mentioned in the legal opinion with the Bank's management. We discussed with the management their intentions in respect of the repossessed asset, reviewed the agreements with lawyers and architects working on resolving the legal restrictions as well as future development of the asset. We assessed the valuation of the assets according to IFRS. We also assessed whether the disclosures in Notes 3(gg), 15 and 19 to the financial statements comply with the IFRS requirements and considered whether the Bank's disclosures on the application of judgement in estimating the recoverable amount and the sensitivity of the results of those estimates reflect the risks associated with impairment of the investment in and loan issued to the subsidiary.

Reporting on other information
Management is responsible for the other information. The other information comprises:

- the Management Report, as set out on pages 3 to 7 of the accompanying Annual Report;
- the Statement on Management Responsibility, as set out on page 8 of the accompanying Annual Report;

but does not include the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon, except as described in the Other reporting responsibilities in accordance with the legislation of the Republic of Latvia section of our report.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed and in light of the knowledge and understanding of the Group and the Bank and their environment obtained in the course of our audit, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Other reporting responsibilities in accordance with the legislation of the Republic of Latvia

We have other reporting responsibilities in accordance with the Law on Audit Services of the Republic of Latvia with respect to the Management Report. These additional reporting responsibilities are beyond those required under the ISAs.

Our responsibility is to consider whether the Management Report is prepared in accordance with the requirements of the Regulation No. 46 "Regulation on the Preparation of Annual Accounts and Annual Consolidated Accounts for Banks, Investment Brokerage Firms and Investment Management Companies" of the Financial and Capital Market Commission of the Republic of Latvia.

Based solely on the work undertaken in the course of our audit, in our opinion:

- the information given in the Management Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Management Report has been prepared in accordance with the requirements of the Regulation No. 46 "Regulation on the Preparation of Annual Accounts and Annual Consolidated Accounts for Banks, Investment Brokerage Firms and Investment Management Companies" of the Financial and Capital Market Commission of the Republic of Latvia.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation of the financial statements that give a true and fair view in accordance with the International Financial Reporting Standards as adopted by the European Union and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Group's and the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group and the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's and the Bank's financial reporting process.

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Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Group's and the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's and the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group and the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

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Other reporting responsibilities and confirmations required by the legislation of the Republic of Latvia and European Union when providing audit services to public interest entities

We were first appointed as auditors of the Group and the Bank on 29th September 2017 by Shareholders of the Bank. Our appointment has been renewed annually by shareholder resolution representing a total period of uninterrupted engagement appointment of 3 years.

We confirm that:

- our audit opinion is consistent with the additional report presented to the Audit Committee of the Bank;
- as stipulated in paragraph 37^6 of the Law on Audit Services of the Republic of Latvia we have not provided to the Group and the Bank the prohibited non-audit services (NASs) referred to in EU Regulation (EU) No 537/2014. We also remained independent of the audited entity in conducting the audit.

The responsible certified auditor on the audit resulting in this independent auditors' report is Diāna Krišjāne.

ERNST & YOUNG BALTIC SIA
Licence No. 17

Diāna Krišjāne
Chairperson of the Board
Latvian Certified Auditor
Certificate No. 124

Riga, 4 March 2020

Consolidated and Bank's Financial Statements

Consolidated and Bank's Statement of Comprehensive Income

	Notes	2019 Group EUR	2019 Bank EUR	2018 Group EUR	2018 Bank EUR
Interest income	5	7,575,945	7,734,139	9,082,132	9,188,907
Interest expense	5	(2,747,097)	(2,747,097)	(3,508,867)	(3,508,867)
Net interest income	5	**4,828,848**	**4,987,042**	**5,573,265**	**5,680,040**
Reversal of allowances for loan impairment	12,13,19,27	1,144,377	1,117,346	890,288	889,592
Net interest income after allowances for loan impairment		**5,973,225**	**6,104,388**	**6,463,553**	**6,569,632**
Fee and commission income	6	4,197,457	4,197,670	6,404,352	6,404,638
Fee and commission expense	6	(455,234)	(455,129)	(789,557)	(789,447)
Net fee and commission income	6	**3,742,223**	**3,742,541**	**5,614,795**	**5,615,191**
Profit/(loss) from sale of financial assets at fair value through profit or loss, net		(213)	(213)	3,569	3,569
Loss from revaluation of securities at fair value through profit or loss, net		22,971	22,971	(4,310)	(4,310)
Profit from derivative financial instruments revaluation, net		32,088	32,088	587,563	587,563
Gain from trading in foreign currencies, net		854,677	854,677	1,988,672	1,988,672
Gain/(loss) from foreign exchange translation, net		170,330	170,330	(573,912)	(573,912)
Other operating income	8	1,278,044	404,880	737,805	584,495
Total operating income		**12,073,345**	**11,331,662**	**14,817,735**	**14,770,900**
Administrative expense	7	(7,814,251)	(7,694,484)	(7,897,409)	(7,791,022)
Amortization and depreciation charges	16,17	(519,574)	(519,574)	(532,930)	(532,930)
Other income		284,237	284,237	374,064	374,064
Other expense	9	(255,263)	(255,263)	(913,083)	(899,276)
Profit before corporate income tax		**3,768,494**	**3,146,578**	**5,848,377**	**5,921,736**
Corporate income tax	10	(149,521)	(149,521)	(216,521)	(216,521)
Net profit for the year attributable to:		**3,618,973**	**2,997,057**	**5,631,856**	**5,705,215**
shareholders of the Bank		3,571,832	2,997,057	5,645,143	5,705,215
non-controlling interests		47,141	-	(13,287)	-
Items that cannot be reclassified subsequently to profit or loss: Gain/(loss) on equity instruments at fair value through other comprehensive income		128,122	128,122	49,141	49,141
Other comprehensive income		**128,122**	**128,122**	**49,141**	**49,141**
Total comprehensive income for the year attributable to:		**3,747,095**	**3,125,179**	**5,680,997**	**5,754,356**
shareholders of the Bank		3,699,954	3,125,179	5,694,284	5,754,356
non-controlling interests		47,141	-	(13,287)	-

The Consolidated and Bank's financial statements on pages 17 through 102 have been approved by the Supervisory Council and the Board of Directors of the Bank and signed on their behalf by:

Aleksandrs Jakovlevs
Chairman of the Board

Yuriy Rodin
Chairman of the Council

Riga, 04 March 2020

The accompanying notes on pages 22 through 102 form an integral part of these financial statements.

Consolidated and Bank's Statement of Financial Position

	Notes	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
Assets					
Cash and balances with the Bank of Latvia	11	113,348,256	113,348,256	95,088,745	95,088,745
Balances due from banks	12	50,350,422	50,350,422	44,132,371	44,132,371
Loans and advances to customers	13	54,754,717	59,297,802	85,498,479	88,260,454
Financial assets at fair value through profit or loss	14	31,015,724	31,015,724	25,249,486	25,249,486
Equity instruments at fair value through other comprehensive income	18	412,205	412,205	284,083	284,083
Derivative financial instruments	25	42,340	42,340	-	-
Intangible assets	16	450,545	450,545	502,886	502,886
Property and equipment, and right-of-use assets	17	13,250,539	13,250,539	13,460,695	13,460,695
Investment in subsidiary	15	-	6,100,000	-	6,100,000
Overpayment of corporate income tax		-	-	278,648	278,648
Other assets	19	24,142,900	11,812,637	18,372,400	9,168,296
Deferred expenses		229,801	229,801	221,050	221,050
Total assets		**287,997,449**	**286,310,271**	**283,088,843**	**282,746,714**
Liabilities					
Deposits from customers	21	221,959,053	222,413,176	217,830,443	217,837,626
Derivative financial instruments	25	-	-	-	-
Other financial liabilities	23	2,052,786	858,117	2,932,204	2,907,608
Deferred income and accrued expense	24	965,571	965,571	933,284	933,284
Debt securities	22	17,896,420	17,896,420	17,558,810	17,558,810
Subordinated loans	34	8,748,647	8,748,647	11,207,357	11,207,357
Current income tax liabilities		1,132	1,132	-	-
Total liabilities		**251,623,609**	**250,883,063**	**250,462,098**	**250,444,685**
Equity					
Share capital	26	32,334,756	32,334,756	32,334,756	32,334,756
Reserves		6	6	6	6
Revaluation reserve on equity instruments at fair value		223,233	223,233	95,111	95,111
Retained earnings		3,281,991	2,869,213	(289,841)	(127,844)
Equity attributable to equity holders of the parent		**35,839,986**	-	**32,140,032**	-
Non-controlling interests		533,854	-	486,713	-
Total equity		**36,373,840**	**35,427,208**	**32,626,745**	**32,302,029**
Total liabilities and equity		**287,997,449**	**286,310,271**	**283,088,843**	**282,746,714**
Off-balance sheet items					
Guarantees issued	27	5,242,483	5,242,483	6,934,513	6,934,513
Financial commitments	27	32,006,395	32,006,395	11,547,703	11,552,260
Assets under management	**35**	**68,177,202**	**68,177,202**	**69,510,343**	**69,510,343**

The Consolidated and Bank's financial statements on pages 17 through 102 have been approved by the Supervisory Council and the Board of Directors of the Bank and signed on their behalf by:

Aleksandrs Jakovlevs
Chairman of the Board

Yuriy Rodin
Chairman of the Council

Riga, 04 March 2020

The accompanying notes on pages 22 through 102 form an integral part of these financial statements.

Consolidated Statement of Changes in Equity

	Attributable to shareholders of the Bank							
	Share capital	Reserves	Retained earnings	Revaluation reserve on available-for-sale financial assets	Revaluation reserve on equity instruments at fair value	Total	Non-controlling interests	Total equity
	EUR	EUR	EUR	EUR	EUR	EUR	EUR	EUR
Balance as at 31 December 2017	**32,334,756**	**6**	**6,850,272**	**45,970**	**-**	**39,231,004**	**-**	**39,231,004**
Impact of adopting IFRS 9	-	-	(5,833,059)	(45,970)	45,970	(5,833,059)	-	(5,833,059)
Restated opening balance under IFRS 9	**32,334,756**	**6**	**1,017,213**	**-**	**45,970**	**33,397,945**	**-**	**33,397,945**
Profit for the year	-	-	5,645,143	-	-	5,645,143	(13,287)	**5,631,856**
Change in the revaluation reserve	-	-	-	-	49,141	49,141	-	49,141
Total comprehensive income for the year	-	-	**5,645,143**	**-**	**49,141**	**5,694,284**	**(13,287)**	**5,680,997**
Dividends declared	-	-	(6,952,197)	-	**-**	(6,952,197)	-	(6,952,197)
Disposal of investment in subsidiary	-	-	-	-	-	-	500,000	500,000
Balance as at 31 December 2018	**32,334,756**	**6**	**(289,841)**	**-**	**95,111**	**32,140,032**	**486,713**	**32,626,745**
Profit for the year	-	-	3,571,832	-	-	3,571,832	47,141	**3,618,973**
Change in the revaluation reserve	-	-	-	-	128,122	128,122	-	128,122
Total comprehensive income for the year	-	-	**3,571,832**	**-**	**128,122**	**3,699,954**	**47,141**	**3,747,095**
Balance as at 31 December 2019	**32,334,756**	**6**	**3,281,991**	**-**	**223,233**	**35,839,986**	**533,854**	**36,373,840**

The accompanying notes on pages 22 through 102 form an integral part of these financial statements.

Bank's Statement of Changes in Equity

	Share capital	Reserves	Retained earnings	Revaluation reserve on available-for-sale financial assets	Revaluation reserve on equity instruments at fair value	Total
	EUR	EUR	EUR	EUR	EUR	EUR
Balance as at 31 December 2017	**32,334,756**	**6**	**6,952,197**	**45,970**	**-**	**39,332,929**
Impact of adopting IFRS 9	-	-	(5,833,059)	(45,970)	45,970	(5,833,059)
Restated opening balance under IFRS 9	**32,334,756**	**6**	**1,119,138**	**-**	**45,970**	**33,499,870**
Profit for the year	-	-	5,705,215	-	-	5,705,215
Change in the revaluation reserve	-	-	-	-	49,141	49,141
Total comprehensive income for the year	-	-	**5,705,215**	**-**	**49,141**	**5,754,356**
Dividends declared	-	-	(6,952,197)	-		(6,952,197)
Balance as at 31 December 2018	**32,334,756**	**6**	**(127,844)**	**-**	**95,111**	**32,302,029**
Profit for the year	-	-	2,997,057	-	-	2,997,057
Change in the revaluation reserve	-	-	-	-	128,122	**128,122**
Total comprehensive income for the year	-	-	**2,997,057**	**-**	**128,122**	**3,125,179**
Balance as at 31 December 2019	**32,334,756**	**6**	**2,869,213**	**-**	**223,233**	**35,427,208**

The accompanying notes on pages 22 through 102 form an integral part of these financial statements.

Consolidated and Bank's Statement of Cash Flows

	Notes	2019 Group EUR	2019 Bank EUR	2018 Group EUR	2018 Bank EUR
Cash flows from/ (used in) operating activities					
Interest received		8,177,937	8,319,671	9,277,373	9,383,754
Interest paid		(2,671,667)	(2,671,576)	(3,542,393)	(3,542,393)
Fees and commission received		4,197,457	4,197,670	6,404,352	6,404,638
Fees and commission paid		(455,234)	(455,129)	(789,557)	(789,447)
Income received from sale of securities at fair value through profit or loss		31,875	31,875	3,157	3,157
Income received from foreign exchange		812,337	812,337	1,989,673	1,989,673
Other operating income received		1,265,084	404,880	735,913	584,043
Personnel expenses paid		(5,858,977)	(5,852,040)	(6,006,872)	(5,996,072)
Administrative and other operating expenses paid		(2,160,814)	(2,097,677)	(2,203,242)	(2,092,296)
Income tax paid		(144,919)	(144,919)	(570,686)	(570,686)
Cash flows generated from operating activities before changes in operating assets and liabilities		**3,193,079**	**2,545,092**	**5,297,718**	**5,374,371**
Changes in operating assets and liabilities					
(Increase)/ decrease in securities at fair value through profit or loss		(5,531,274)	(5,531,274)	36,649,804	36,649,804
(Increase)/ decrease in balances due from banks		432,159	432,159	4,480,395	4,480,395
(Increase)/ decrease in loans and advances to customers, net		33,573,512	31,780,955	22,496,240	22,234,797
(Increase)/ decrease in other assets		(4,315,224)	(1,317,620)	(2,348,949)	(1,823,228)
Increase/ (decrease) in deposits from customers, net		2,128,999	2,575,939	(84,866,578)	(85,207,509)
Increase/ (decrease) in other liabilities, net		1,957,937	953,937	(13,279,254)	(13,279,254)
Net cash flows (used in) operating activities		**31,439,188**	**31,439,188**	**(31,570,624)**	**(31,570,624)**
Cash flows to/ from investing activities					
Proceeds from partial sale of investment in subsidiary		-	-	503,788	503,788
Purchase of intangible assets		(99,034)	(99,034)	(91,548)	(91,548)
Purchase of property and equipment		(30,190)	(30,190)	(10,155)	(10,155)
Net cash flows generated from /(used in) investing activities		**(129,224)**	**(129,224)**	**402,085**	**402,085**
Cash flows to/ from financing activities					
Dividends paid		(2,656,244)	(2,656,244)	(4,295,953)	(4,295,953)
Repayment of the Subordinated loans		(2,694,576)	(2,694,576)	-	-
Repayment of the principal amount of lease liabilities		(35,038)	(35,038)	-	-
Net cash flows generated from /(used in) financing activities		**(5,385,858)**	**(5,385,858)**	**(4,295,953)**	**(4,295,953)**
Effect of exchange rates on cash and cash equivalents		(797,635)	(797,635)	(1,915,485)	(1,915,485)
Net increase/(decrease) in cash and cash equivalents		**25,126,471**	**25,126,471**	**(37,379,977)**	**(37,379,977)**
Cash and cash equivalents at the beginning of the year	20	139,178,499	139,178,499	176,558,476	176,558,476
Cash and cash equivalents at the end of the year	**20**	**164,304,970**	**164,304,970**	**139,178,499**	**139,178,499**

The accompanying notes on pages 22 through 102 form an integral part of these financial statements.

Notes to the financial statements

1. Incorporation and principal activities

AS Reģionālā investīciju banka (hereinafter – the Bank) provides financial services to corporate customers and private individuals. The Bank established the following representative offices: in Odessa, Ukraine, in 2005; in Dnipro (Dnepropetrovsk), Ukraine, in 2007; in Kiev, Ukraine, at the beginning of 2009, and, in Brussels, the capital of Belgium, in 2010. On 12 December 2018, after the changes in the client base of the Bank and in the course of optimization of the expenses, the Board of the Bank adopted a decision on the liquidation of representative offices in Kiev and Dnipro (Ukraine).

In August 2016, the Bank established a 100% subsidiary - the limited liability company *Grunewald Residence*, reg. No 40203014344, whose share capital is EUR 6,600,000. On 19 December 2018, there were sold 500,000 of the company's shares to a third party, as a result total direct Bank's investment into this subsidiary as at 31 December 2019 was 92.42%.

The Bank and the limited liability company *Grunewald Residence* together form a group (hereinafter - the Group), operating in the area of financial services and real estate.
The legal and office address of the Bank is:
J.Alunāna Street 2
LV-1010, Riga
Latvia

The legal and office address of SIA *Grunewald Residence* is:
J. Alunāna Street 2
LV-1010, Riga
Latvia

The Bank has no other representative offices, subsidiaries or other entities, except for the above.

These financial statements were approved for issue by the Bank's Council and Board of Directors on 04 March 2020.

2. Operating environment of the Group and the Bank

Operations of the Bank are affected by tendencies in Ukrainian market, as the parent of the Bank is a Ukrainian public joint stock company – the bank *Pivdennij*, as well as significant portion of the loans issued by the Bank have been issued to Ukrainian companies and companies whose business is related to Ukraine.
The table below presents the total risk exposure of the Bank and the Group in Ukraine as at 31 December 2019 and 31 December 2018:

	31.12.2019 Group EUR '000	31.12.2019 Bank EUR '000	31.12.2018 Group EUR '000	31.12.2018 Bank EUR '000
Statement of financial position assets subject to Ukraine country risk:				
Balances due from banks	5,487	5,487	3,309	3,309
Loans issued and other receivables	21,823	21,823	36,101	36,101
Total	**27,310**	**27,310**	**39,410**	**39,410**
Off-balance sheet items subject to the Ukraine country risk:				
Off-balance sheet financial commitments	15,447	15,447	1,953	1,953
Total	**15,447**	**15,447**	**1,953**	**1,953**

2. Operating environment of the Group and the Bank *(cont'd)*

In 2019, the recovery of Ukrainian economy continued. The Central Bank of Ukraine increased foreign currency reserves and contained inflation below a 10% level; the government debt-to-GDP ratio continued to decrease. The new government is committed to improve the business environment and to abolish the moratorium on the sale of agricultural land. These measures might attract greater foreign investments in Ukraine, facilitating further economic growth.

The transformation of the Ukrainian economic structure continues. The manufacturing sector registered a decline in the first eleven months of 2019; however, there was a considerable increase in the agricultural output which was partly due to good yield. The construction sector had still good results and there was also an increase in the financial and insurance sectors. Added value rose faster in the sectors where the growth is mainly driven by consumer demand. Due to rising per capita income, the retail volumes also continued to grow.

An important event in 2019 was the approval of the Public Debt Management Strategy 2022 aimed at reducing the public debt from 52% to 43% of GDP. By implementing the strategy, the government intends not only to reduce the debt in absolute terms but also to considerably improve its credit rating and thus obtain loans on more favorable terms and for a longer period of time. So far Ukraine has to re-borrow as the national economy is not able to satisfy the development needs. In the previous year, the government reached an agreement on a new cooperation program with the major creditor – the International Monetary Fund; however, to commence it, Ukraine must meet several conditions. Further negotiations on the new program amounting to approximately USD 5.5 billion are planned in the first quarter of 2020.

Preliminary data suggest that in comparison with the previous year the GDP grew by 2.5% in the first quarter, by 4.6% – in the second quarter and by 4.1% – in the third quarter. At the same time, inflation gradually decreased compared with the previous year (9.8%). The projected inflation at the end of 2019 was 6.3%, and the GDP forecasts for 2019 varied at the 3.2-3.6% level.

In 2019, the Ukrainian banking sector showed high profit figures; however, its loan portfolio quality was still an issue. In April 2019, the non-performing loans (NPL) accounted for 51.7% of all loans. The non-performing loans of public banks accounted for approximately 70% of all NPL of the whole banking sector. The further government strategy regarding these banks includes gradual repairing and partly privatization of at least two of the four public banks - *Oschadbank* and *PrivatBank*.

Regarding the future economic prospects, GDP is expected to remain at the 3.6% level in 2020. Inflation for 2020 is projected around 5.4%. In September 2019, the international rating agencies *Fitch and Standard & Poor's* upgraded Ukrainian sovereign credit rating by one degree to B with a stable outlook.

Impact on borrowers

The solvency of the borrowers of the Bank may be affected by the reduction of their liquidity. 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. To the extent of the available information, the management has properly reflected the revised estimates of expected future cash flows in its impairment assessments.

2. Operating environment of the Group and the Bank *(cont'd)*

Impact on collateral

The amount of allowance for impaired loans is based on the management's appraisals of these assets at the reporting date after taking into consideration the cash flows that may result from foreclosure less costs for obtaining and selling the collateral. As a result of possible economy downturn, the actual realizable value on foreclosure may differ from the value used in estimating the allowances for impairment.

3. Summary of significant accounting policies

A summary of significant accounting policies of the Group and the Bank, all of which were applied consistently throughout 2019 and 2018, are set out below:

(a) Changes in accounting policies

The Group and the Bank applied IFRS 16 for the first time. The nature and effect caused by the adoption of the new accounting standard are described below.

The Group and the Bank for the first time applied certain amendments to standards effective for annual periods beginning on or after 1 January 2019. The Group and the Bank have not applied any standards, interpretations or amendments which are issued, but not yet effective and not early adopted. The nature and effect of each amendment are disclosed below:

IFRS 16 Leases

As of 1 January 2019, IFRS 16 has superseded IAS 17 *Leases*, IFRIC 4 *Determining whether an Arrangement contains a Lease*, SIC-15 *Operating Leases-Incentives* and SIC-27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*. The standard sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to recognize most leases on the balance sheet. Lessor accounting under IFRS 16 is substantially unchanged from IAS 17. Lessors will continue to classify leases as either operating or finance leases using similar principles as in IAS 17. IFRS 16 did not have an impact on leases where the Group and the Bank are the lessors.

The Group and the Bank have adopted IFRS 16 using the modified retrospective approach of adoption with the date of initial application of 1 January 2019. Under this method, the standard is applied retrospectively with the cumulative effect of initially applying the standard is recognized in retained earnings at the date of initial application and comparative information is not restated.

The Group and the Bank elected to use the transition practical expedient to not reassess whether a contract is or contains a lease at 1 January 2019. Instead, the Group and the Bank applied the standard only to contracts that were previously identified as leases applying IAS 17 and IFRIC 4 at the date of initial application.

As of 1 January 2019, the Group and the Bank have recognized the right-of-use assets amounting to EUR 109,845 and lease liabilities of EUR 109,845, which did not result in any impact on the retained earnings of the Group and the Bank.

The Group and the Bank have effective lease agreements for premises. Before the adoption of IFRS 16, the Group and the Bank (as lessees) classified each lease agreement as an operating lease at the agreement date. Information about the accounting policy applied before 1 January 2019 is provided in Note (s) 'Leases'.

3. Summary of significant accounting policies *(cont'd)*

(a) Changes in accounting policies *(cont'd)*

After the adoption of IFRS 16, the Group and the Bank applied a single recognition and measurement approach for all leases, except for short-term leases and leases of low-value assets. Information about the accounting policy applied before 1 January 2019 is provided in Note (s) 'Leases'. The standard provides specific transition requirements and practical expedients, which have been applied by the Group and the Bank.

Leases previously classified as operating leases

The Group and the bank recognized right-of-use assets and lease liabilities for those leases previously classified as operating leases, except for short-term leases and leases of low-value assets. Lease liabilities were measured at the present value of the remaining lease payments, discounted using the Group and the Bank's incremental borrowing rate at the date of initial application, i.e. 1 January 2019. The right-of-use assets were measured at an amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognised in the statement of financial position immediately before the date of initial application – the Group applied this approach to all leases of premises

The Group also applied the available practical expedients wherein it:

- used a single discount rate to a portfolio of leases with reasonably similar characteristics;
- applied the short-term leases exemptions to leases with lease term that ends within 12 months of the date of initial application;
- used hindsight in determining the lease term where the contract contained options to extend or terminate the lease.

The lease liabilities as at 1 January 2019 can be reconciled to the operating lease commitments on the basis of the average interbank credit interest rates determined by the national banks of Ukraine and Latvia on 31 December 2018, as follows:

	EUR
Operating lease commitments as at 31 December 2018	**115,634**
Weighted average incremental borrowing rate as at 1 January 2019:	
– lease asset in Ukraine	18%
– lease asset in Latvia	0%
Commitments relating to short-term leases	5,788
Lease liabilities as at 1 January 2019	**109,846**

(b) Reporting currency

The financial statements are prepared in the euros (EUR), unless stated otherwise. The functional and presentation currency of the Bank and its subsidiary is the euro.

(c) Basis of preparation

The financial statements are prepared in accordance with International Financial Reporting Standards as adopted by the European Union (hereinafter - IFRS), on a going concern basis. In preparation of the financial statements on a going concern basis, the management considered the Group and Bank's financial position, access to financial resources and analyzed the impact of the recent financial crisis on the future operations of the Group and the Bank.

The financial statements have been prepared on a historical cost basis, except for financial assets at fair value through other comprehensive income and derivative financial instruments that are measured at fair value.

3. Summary of significant accounting policies *(cont'd)*

(c) Basis of preparation *(cont'd)*

The preparation of financial statements in conformity with IFRS 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, the actual results ultimately may differ from those estimates. The same accounting policies were used consistently in the preparation of the financial statements for the year 2019, if compared to those of 2018 except for IFRS 16.

(d) Basis of consolidation

Subsidiaries, namely, the companies, in which the Group directly or indirectly has the power to govern the financial and operating policies as well as the reallocation of income, are consolidated in the Group's financial statements. Investments in subsidiaries in the Bank's financial statements are stated at cost less impairment, if any). Subsidiaries are consolidated from the date on which control is transferred to the Group and excluded from the consolidated financial statements from the date that control ceases. Acquisition of subsidiaries is accounted for using the purchase method. The acquisition cost comprises the assets transferred, shares issued or liabilities taken over at fair value as at the purchase date, plus costs directly attributable to the acquisition. The excess of the net assets purchased over the purchase price is recorded as a goodwill. All intra-group transactions and balances and unrealized gains resulting from intra-group transactions are eliminated. Unrealized losses are also eliminated, except where costs cannot be recovered. Accounting policies of subsidiaries are changed where necessary to ensure consistency with the policies adopted by the Group.

(e) Fair value measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability; or
- In the absence of a principal market, in the most advantageous market for the asset or liability.

The principal or the most advantageous market must be accessible by the Group and the Bank. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest. A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Group and the Bank use valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs. All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorized within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

Level 1 — Quoted (unadjusted) market prices in active markets for identical assets or liabilities;

Level 2 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable;

3. Summary of significant accounting policies *(cont'd)*

(e) Fair value measurement *(cont'd)*

Level 3 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

For assets and liabilities that are recognized in the financial statements at fair value on a recurring basis, the Group and the Bank determine whether transfers have occurred between levels in the hierarchy by re-assessing categorization (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

(f) Initial recognition

Date of recognition

Regular way purchase or sale of financial assets is recognized on a trade date, i.e., on the date when the Group and the Bank entity commits themselves to purchase an asset or liability. Regular way purchase or sale is a purchase or sale of a financial asset under a contract whose terms require delivery of the asset within the time frame established generally by regulation or convention in the marketplace concerned.

Initial measurement

The classification of financial instruments at initial recognition depends on the financial instrument's contractual terms and the business model selected for managing them. Financial instruments, except financial assets and financial liabilities stated at fair value through profit or loss, are initially measured at fair value plus or minus transaction costs.

Measurement categories of financial assets and liabilities

In accordance with IFRS 9, all debt-based financial assets which do not meet the 'solely payments of principal and interest' criterion, at initial recognition are measured at fair value through profit or loss. Under this criterion, the debt instruments which are not in line with 'basic lending arrangement', e.g., instruments which contain embedded conversion options or non-recourse loans, are measured at fair value through profit or loss. Debt-based financial assets which do meet the 'solely payments of principal and interest' criterion, at initial recognition are measured on the basis of a business model under which the instruments are managed:

- Instruments managed under the 'hold to collect' business model are measured at amortized cost;
- Instruments managed under the 'hold to collect and sell' business model are measured at fair value through other comprehensive income;
- Instruments managed under other business models, including financial assets held for trading, are measured at fair value through profit or loss.

Equity instruments at initial recognition are measured at fair value through profit or loss, unless the financial asset is not irrevocably designated at fair value through other comprehensive income.

Regarding capital expenditures at fair value through other comprehensive income, all realized and unrealized gains and losses, excluding income from dividends, are recognized in other comprehensive income as items that cannot be reclassified subsequently to profit or loss.

The Group and the Bank classify all financial assets depending on the business model selected for managing assets and the asset's contractual terms, which are measured:

- at amortized cost;
- at fair value through OCI;
- at fair value through profit or loss.

3. Summary of significant accounting policies *(cont'd)*

(f) Initial recognition *(cont'd)*

The Group and the Bank classify and measure derivative financial instruments and financial assets held for trading at fair value through profit or loss. The Group and the Bank may measure financial instruments at fair value through profit or loss if such measurement eliminates or significantly reduces a measurement or recognition inconsistency.

Financial liabilities, other than loans and borrowings and financial guarantees, are measured at amortized cost or at fair value through profit or loss if held for trading or are derivative financial instruments

Balances due from banks, loans to customers, investments in securities at amortized cost

The Group and the Bank only measure the balances due from banks, loans to customers and other financial investments at amortized cost when both of the following conditions are met:

- a financial asset is held under a business model whose objective is to hold assets to collect contractual cash flows;
- the contractual cash flows of an asset give rise to payments on specified dates that are solely payments of principal and interest (SPPI) on the principal amount outstanding.

A more detailed information on the above conditions is provided below.

Business model assessment

The Group and the Bank determine the business model at a level that reflects the way groups of financial assets are managed together to achieve a particular business objective.

The business model of the Group and the Bank is not determined on an instrument-by-instrument basis, rather it is assessed at a higher level of aggregated portfolios and is based on observable evidence, for example:

- how the performance of the business model and the financial assets held within that business model are evaluated and reported to the entity's key management personnel;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and the way those risks are managed;
- how managers of the business are compensated – e.g., whether the compensation is based on the fair value of the assets managed or the contractual cash flows collected;
- the expected frequency, volume and timing of sales also are significant aspects to be considered in the assessment carried out by the Group and the Bank.

The assessment of a business model is performed on the basis of scenarios that are reasonably expected to occur, excluding 'worst case' or 'stress case' scenarios. If cash flows, subsequent to initial recognition, are realized in a way that is different from the Group and Bank's initial expectations, the Group and the Bank do not change the classification of the remaining financial assets held in that business model, but consider this information in assessing the business model for newly generated or newly acquired financial assets newly generated or newly purchased financial assets.

SPPI test

As a second step in determining the appropriate classification category the Group and the Bank assess the financial asset's contractual terms in order to determine whether the financial asset meets the SPPI test.

For the purpose of this test, a principal is defined as fair value of a financial asset at initial recognition, which may change over the life of a financial instrument (for example, if there are repayments of principal or amortization of premium/discount).

In a lending arrangement, most significant interest components usually are consideration for the time value of money and credit risk. For the SPPI test purposes, the Group and the Bank applies judgment and considers relevant factors such as the currency in which the financial asset is denominated and the period for which the interest rate is set.

3. Summary of significant accounting policies *(cont'd)*

(f) Initial recognition *(cont'd)*

In contrast, contractual terms that introduce a more than de minimis exposure to risks or volatility in the contractual cash flows that is unrelated to a basic lending arrangement, do not give rise to contractual cash flows that are solely payments of principal and interest on the principal amount outstanding. In such cases the financial asset is measured at fair value through profit or loss.

Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets held for trading and those designated at fair value through profit or loss. Financial assets at fair value through profit or loss comprise debt securities held by the Group and the Bank for trading purposes. They are accounted for at fair value with all gains and losses from revaluation and trading reported in the statement of comprehensive income. Interest earned while holding trading securities is reported as interest income.

All regular way purchases and sales of financial assets held for trading are recognized at trade date, which is the date that the Group and the Bank commit to purchase or sell the asset.

Financial assets are derecognized when the rights to receive cash flows from the financial assets have expired or where the Group and the Bank have transferred substantially all risks and rewards of ownership.

Debt instruments measured at fair value through other comprehensive income (FVTOCI)

The Group and the Bank, in accordance with IFRS 9, apply a classification to debt instruments measured at FVTOCI when both of the following conditions are met:

- an instrument is held within a business model whose objective is to hold financial assets in order to collect contractual cash flows and sell financial assets;
- the financial asset's contractual terms meet the SPPI test.

Debt instruments designated at FVTOCI are subsequently measured at fair value recognizing gain or loss resulting from changes in the fair value in other comprehensive income. For debt instruments at fair value through FVTOCI, interest income and foreign exchange gain or loss are recognized in the statement of profit or loss and computed in the same manner as for financial assets measured at amortized cost. Upon derecognition, the cumulative fair value change recognized in OCI is recycled to profit or loss.

Expected credit loss (ECLs) on debt instruments measured at FVTOCI do not reduce the carrying amount of these financial assets in the statement of financial position, which remains at fair value. Instead, an amount equal to an allowance, which would be established if the assets were measured at amortized cost, is recognized in other comprehensive income as 'accumulated impairment amount', with a corresponding amount debited to the statement of profit or loss. Other accumulated loss recognized in other comprehensive income is taken to the statement of profit or loss upon derecognition of the respective asset.

Equity instruments measured at FVTOCI

The Group and the Bank, upon initial recognition, often elect to classify irrevocably its equity investments as equity instruments designated at fair value through OCI when they meet the definition of equity under IAS 32 *Financial Instruments: Presentation* and are not held for trading. The classification is determined on an instrument-by-instrument basis.

Gains and losses on these financial assets are never recycled to profit or loss. Dividends are recognized as other income in the statement of profit or loss when the right of payment has been established, except when the Group benefits from such proceeds as a recovery of part of the cost of the financial asset, in which case, such gains are recorded in other comprehensive income. Equity instruments designated at FVTOCI are not subject to impairment assessment. Upon disposal of these instruments, any remaining balance in the revaluation reserve relating to the asset disposed of is transferred directly to retained earnings.

3. Summary of significant accounting policies *(cont'd)*

(f) Initial recognition *(cont'd)*

Financial guarantees, letters of credit and undrawn loan commitments

The Group and the Bank provide financial guarantees, letters of credit and loan commitments. Financial guarantees, namely, premiums received, are initially recognized in the financial statements at fair value. After initial recognition, the Group's and Bank's liabilities arising from guarantees are measured at the higher of the amount initially recognized less cumulative amortization recognized in the statement of profit or loss, and under IFRS 9 – according to the forward-looking ECL model.

Undrawn loan commitments and letters of credit are liabilities whereby the Group and the Bank, during the commitment period, must issue a loan to the customer under agreed upon terms. Allowances for financial guarantee contracts were established, as in case of onerous contracts; under IFRS 9 these contracts are subject to the ECL model.

(g) Income and expense recognition

Interest income and expense are recognized in the statement of comprehensive income for all interest-bearing instruments on an accrual basis using the effective interest method.

The effective interest method is a method for calculating the amortized cost of a financial asset or a financial liability based on the recognition of interest income or interest expense over the relevant period

The Group and the Bank calculate interest revenue on debt financial assets measured at amortized cost or at FVOCI by applying the EIR to the gross carrying amount of financial assets other than credit-impaired assets. When a financial asset becomes credit-impaired, the Group and the Bank calculate interest revenue by applying the effective interest rate to the net amortized cost of the financial asset. If the financial assets cure and are no longer credit-impaired, the Group and the Bank revert to calculating interest revenue on a gross basis.

Commissions received or incurred in respect of origination of financial assets or funding are deferred and recognized as an adjustment to the effective interest rate applied to the asset or liability. Commissions on servicing of settlement accounts are recognized in the statement of comprehensive income on a regular basis throughout the duration of the customer contract. Other fees and commissions, including those related to trust activities, are credited and/or charged to the statement of comprehensive income as earned / incurred.

(h) Foreign currency translation

Functional and presentation currency

The functional currency of the Bank and the Group companies is the currency of the primary economic environment in which the Group and the Bank operate. The financial statements are presented in the euros (EUR), which is the Bank's functional and the Group's presentation currency.

Transactions and balances

Foreign currency transactions have been translated into the euro applying the rate determined by the conversation procedure between central banks of the European System of Central Banks and other central banks and which is published on the European Central Bank's website. To those foreign currencies, for which the ECB does not publish the EUR reference rate, the foreign currency exchange rates published by Bloomberg are applied. Any gain or loss resulting from a change in exchange rates is included in the statement of comprehensive income as profit or loss from revaluation of foreign currency positions.

During the preparation of the financial statements of the Group and the Bank, the most commonly used currency exchange rates (foreign currency units against one EUR) were as follows:

Reporting date	USD
31 December 2019	1.1234
31 December 2018	1.1450

3. Summary of significant accounting policies *(cont'd)*

(i) Income taxes

Income taxes include current and deferred taxes.

Legal entities have not been required to pay income tax on earned profits starting from 1 January 2018 in accordance with amendments made to the Corporate Income Tax Law of the Republic of Latvia. Corporate income tax is paid on distributed profits and deemed profit distributions. Consequently, current and deferred tax assets and liabilities are measured at the tax rate applicable to undistributed profit.

Starting from 1 January 2018, both distributed profits and deemed profit distributions have been subject to the tax rate of 20 per cent of their gross amount, or 20/80 of net expense. Corporate income tax on dividends is recognized in the consolidated statement of profit or loss as expense in the reporting period when respective dividends are declared, while, as regards other deemed profit items, at the time when expense is incurred in the reporting year. No provision is recognized for income tax payable on a dividend distribution before dividends are declared but information on the contingent liability is disclosed in the notes to the consolidated financial statements.

(j) Deferred tax assets and liabilities

Deferred tax is provided using the liability method for all temporary differences arising between the tax bases of assets and liabilities and their carrying value for accounting purposes. Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realized or the liability is settled, based on tax rates that have been enacted or substantively enacted by the balance sheet date. Deferred tax assets are recognized to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, associates and joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Additional income taxes that arise from the distribution of dividends are recognized at the same time as the liability to pay the related dividend is recognized.

(k) Cash and cash equivalents

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

(l) Due from other 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 amortized cost.

(m) Loans and allowances for loan impairment

The Group and Bank only measure amounts due from credit institutions, loans to customers and other financial investments at amortized cost if both of the following conditions are met:

- The financial asset is held within a business model with the objective to hold financial assets in order to collect contractual cash flows;
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding (SPPI).

3. Summary of significant accounting policies *(cont'd)*

(m) Loans and allowances for loan impairment *(cont'd)*

Forborne exposures

The Group and the Bank derecognize a financial asset, e.g., a loan to customer, if a new agreement has been reached on such terms and conditions of the loan that it actually becomes a new. Forborne exposures are debt contracts regarding which forbearance measures have been applied. Forbearance measures consist of concessions to a debtor that is experiencing or about to experience difficulties in meeting its financial commitments ('financial difficulties'). Forborne exposures are classified under Stage 2 for the ECL assessment purposes.

In order to decide whether forborne loans are to be classified as Stage 3 assets for ECL assessment purposes, the Bank assesses the following:
- The adequacy and observance of the loan payment schedule (initial and further payment schedules), which, inter alia, includes a repeated non-observance of the payment schedule, changes in the payment schedule in order to avoid any delays, or the payment schedule is based on forecasts which are not based on macroeconomic forecasts or realistic assumptions regarding the borrower's capability of repaying debt obligations;
- Whether the loan agreement includes terms which postpone the deadline of regular repayments in a way that hinders the assessment of conformity to the set classification, for example, if the repayment periods of the principal amount are postponed for more than two years.

Other criteria for forborne loans to be classified as Stage 3 assets are:
- Loan forbearance which will most likely diminish financial commitments;
- New forbearance measures are set for a forborne exposure;
- The number of days past due for a forborne exposure exceeds 30 days;
- The borrower is classified as unlikely to pay.

If there are changes which do not result in derecognition, the Group and the Bank also reassess whether there is no significant increase in credit risk and whether the assets should be classified as credit-impaired assets. If the assets are classified as credit-impaired assets they will remain under Stage 3 at least for a 12-month trial period to be reclassified to Stage 2, and 24-months to be reclassified to Stage 1. The forborne exposure is to be reclassified out of Stage 3 if regular payments of more than an insignificant amount of principal or interest have been made during the second half of the probation period.

(n) Sale and repurchase agreement

Sale and repurchase agreements are accounted for as financing transactions. Under sale and repurchase agreements, where the Group and the Bank are transferors, assets transferred remain on the Group and Bank's statement of financial position and are subject to the Group and Bank's usual accounting policies, with the purchase price received included as a liability owed to the transferee. Where the Bank is a transferee, the assets are not included in the Group and Bank's statement of financial position, but the purchase price paid by it to the transferor is included as an asset. Interest income or expense arising from outstanding sale and repurchase agreements is recognized in the statement of comprehensive income over the term of the agreement using the effective interest method.

(o) Derivative financial instruments

Derivative financial instruments comprise various derivatives, inter alia, options, forwards, futures and foreign currency and capital market transactions. Such financial instruments are held for trading and stated at fair value. Fair values are based on quoted market prices or pricing models where the actual market or contractual prices of the existing instruments as well as other factors are considered.

3. Summary of significant accounting policies *(cont'd)*

(o) Derivative financial instruments *(cont'd)*

All derivatives are carried as financial assets when fair value is positive and as financial liabilities when fair value is negative. Any gain or loss arising from these instruments is taken to the statement of profit or loss as net gain/ (loss) from financial instruments designated at fair value through profit or loss or as foreign currency exchange gain/ (loss) depending on the nature of the respective instrument.

An embedded derivative is a component of a hybrid (combined) instrument that also includes a non-derivative host contract—with the effect that some of the cash flows of the combined instrument vary in a way similar to a stand-alone derivative. An embedded derivative causes some or all of the cash flows that otherwise would be required by the contract to be modified according to a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract. A derivative that is attached to a financial instrument but is contractually transferable independently of that instrument, or has a different counterparty from that instrument, is not an embedded derivative, but a separate financial instrument.

This is the way in which the Group and the Bank account for derivatives embedded in financial liabilities and non-derivative host contracts. The classification of financial assets is based on the business model and SPPI assessment, without separation of embedded derivatives (see also note 3).

(p) Repossessed collateral

Repossessed collateral represents real estate repossessed by the Group and the Bank for the purpose of selling as collateral for the outstanding loans and is disclosed under other non-financial assets. The repossessed real estate is stated at inventories at lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs necessary to make the sale.

(q) Intangible assets

The acquired computer software licenses are recognized as intangible assets at cost, including any expenditure that is directly attributable to preparing the asset for its intended use. Intangible assets are amortized over their estimated useful lives, not exceeding 5 years, on a straight-line basis.

(r) Property and equipment

The items of property and equipment are stated at cost less accumulated depreciation and impairment. The cost includes expenditure directly attributable to the acquisition of the asset.

Subsequent costs are included in the asset's carrying amount or recognized 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 Bank and the cost of the item can be measured reliably.

Such costs are depreciated over the asset's remaining useful life. All other repairs and maintenance are charged to the statement of comprehensive income during the financial period in which they are incurred.

Depreciation is calculated on a straight-line basis over the estimated useful life of the asset to write down the cost of property and equipment to their residual values at the end of the useful life. The estimated useful lives are, as follows:

Land	is not depreciated
Building	50 years
Office equipment	10 years
Computers	3 years
Transport vehicles	5 years

3. Summary of significant accounting policies *(cont'd)*

(r) Property and equipment *(cont'd)*

Buildings and land under the property and equipment category are measured at a revalued amount. The revalued amount is the fair value at the revaluation date less subsequent accumulated depreciation and impairment loss. The fair value of land and buildings is determined from market-based evidence by appraisal that is normally undertaken by professionally qualified valuers at the end of the reporting year. Revaluation gains are recorded under the heading of revaluation surplus and recognized in other comprehensive income. A revaluation loss is initially taken to the revaluation surplus (and recorded in other comprehensive income) related to these assets, if any, and subsequently included in profit or loss for the reporting period (see Note 17).

The carrying values of property and equipment (except for the buildings and land) are reviewed for impairment on a periodical basis. Where the carrying value of an asset exceeds the estimated recoverable amount and the respective changes in the value are not considered to be temporary, the value of the corresponding asset is written down to its recoverable amount. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the statement of comprehensive income.

(s) Leases

The Group and the Bank as lessees

As of 1 January 2019, the Group and the Bank have assessed at contract inception whether a contract is, or contains, a lease. That is, if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

The Group and the Bank apply a single recognition and measurement approach for all leases, except for short-term leases and leases of low-value assets. The Group and the Bank recognize lease liabilities to make lease payments and right-of-use assets representing the right to use the underlying assets.

Right-of-use assets

As of 1 January 2019, the Group and the Bank have recognized right-of-use assets at the commencement date of the lease (i.e., the date the underlying asset is available for use). Right-of-use assets are measured at cost, less any accumulated depreciation and impairment losses, and adjusted for any remeasurement of lease liabilities. The cost of right-of-use assets includes the amount of lease liabilities recognized, initial direct costs incurred, and lease payments made at or before the commencement date less any lease incentives received. Right-of-use assets are depreciated on a straight-line basis over the shorter of the lease term and the estimated useful lives of the assets, which for the lease of premises is 3 to 5 years.

If ownership of the leased asset transfers to the Group at the end of the lease term or the cost reflects the exercise of a purchase option, depreciation is calculated using the estimated useful life of the asset. The right-of-use assets are also subject to impairment (see Note 17).

Lease liabilities

As of 1 January 2019, at the commencement date of the lease, the Group and the Bank have recognized lease liabilities measured at the present value of lease payments to be made over the lease term. The lease payments include fixed payments (including in-substance fixed payments) less any lease incentives receivable, variable lease payments that depend on an index or a rate, and amounts expected to be paid under residual value guarantees. The lease payments also include the exercise price of a purchase option reasonably certain to be exercised by the Group and the Bank and payments of penalties for terminating the lease, if the lease term reflects the Group and the Bank exercising the option to terminate.

3. Summary of significant accounting policies *(cont'd)*

(s) Leases *(cont'd)*

Variable lease payments that do not depend on an index or a rate are recognized as expenses (unless they are incurred to produce inventories) in the period in which the event or condition that triggers the payment occurs. In calculating the present value of lease payments, the Group and the Bank use their incremental borrowing rate at the lease commencement date because the interest rate implicit in the lease is not readily determinable. After the commencement date, the amount of lease liabilities is increased to reflect the accretion of interest and reduced for the lease payments made. In addition, the carrying amount of lease liabilities is remeasured if there is a modification, a change in the lease term, a change in the lease payments (e.g., changes to future payments resulting from a change in an index or rate used to determine such lease payments) or a change in the assessment of an option to purchase the underlying asset.

The Group's lease liabilities are disclosed under other financial liabilities (see Note 23).

Short-term leases and leases of low-value assets

The Group and the Bank apply the short-term lease recognition exemption to their short-term leases of machinery and equipment (i.e., those leases that have a lease term of 12 months or less from the commencement date and do not contain a purchase option). They also apply the lease of low-value assets recognition exemption to leases of office equipment that are considered to be low value. Lease payments on short-term leases and leases of low-value assets are recognized as expense on a straight-line basis over the lease term.

Before 1 January 2019, the Group and the Bank as lessees classified leases that transfer substantially all of the risks and rewards of ownership as finance leases and all other leases as operating leases. In case of finance leases, upon initial recognition the leased assets were measured at an amount equal to the lower of their fair value and the present value of the minimum lease payments. Subsequently, the assets were accounted for in accordance with the accounting policy applicable to that asset. Assets held under operating leases were not recognized in the Group and Bank's statements of financial position. Instead, payments made under such leases were recognized in profit or loss on a straight-line basis over the term of the lease.

The Group and the Bank as lessors

As lessors, the Group and the Bank determine at lease inception whether the lease is a finance lease or an operating lease. If the Group and the Bank determine that the lease transfers substantially all of the risks and rewards of ownership of the underlying asset, the lease is a finance lease. Leases in which the Group and the Bank do not transfer substantially all the risks and rewards incidental to ownership of an asset are classified as operating leases. Rental income arising is accounted for on a straight-line basis over the lease terms and is included in revenue in the statement of profit or loss due to its operating nature. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognized over the lease term on the same basis as rental income. Contingent rents are recognized as revenue in the period in which they are earned.

The accounting policies applied by the Group as a lessor in the comparative period were not different from IFRS 16.

(t) Derecognition of financial assets and liabilities

Financial assets (or, where applicable, a portion of a financial asset or a part of a group of similar assets) are recognized when:

- the contractual rights to the cash flows from the financial asset have expired;

3. Summary of significant accounting policies *(cont'd)*

(t) Derecognition of financial assets and liabilities *(cont'd)*

- the Group and the Bank have transferred the contractual rights to the cash flows from the financial asset or retain the contractual rights to the cash flows from the financial asset, but assume an obligation to pay the received cash flows in full without material delay to a third party under a pass-through arrangement; and
- either (a) the Group and the Bank have transferred substantially all the risks and rewards of the asset, or (b) the Group and the Bank have neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Financial assets are written off, in full or in part, only when the Group and the Bank have no reasonable expectation of recovery. If the amount to be written off exceeds the cumulative loss amount, the difference is first considered as increase in allowance which then is set off against the gross carrying amount. Any further recovery is included in credit loss expense. A write-off constitutes a derecognition event. Financial liabilities are derecognized when the obligation specified in the contract is either discharged or cancelled or expires. Where there has been an exchange between an existing borrower and lender of debt instruments with substantially different terms, or there has been a substantial modification of the terms of an existing financial liability, this transaction is accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. A gain or loss from extinguishment of the original financial liability is recognized in profit or loss (see also note 3(m)).

(u) Deposits from customers

Deposits from customers are non-derivative liabilities to individuals, state or corporate customers and are carried at amortized cost.

(v) Borrowings

Borrowings are recognized initially at fair value net of transaction costs incurred. Borrowings are subsequently stated at amortized cost and any difference between net proceeds and the redemption value is recognized in the statement of comprehensive income over the period of the borrowings using the effective interest method.

(w) Debt securities issued

The Group and the Bank recognize the issued debt securities at the date when the respective funds are received. After initial recognition when these financial liabilities are stated at fair value, including direct transaction costs, those are subsequently carried at amortized cost using the effective interest method. When issued debt securities are sold at a discount, the difference is amortized applying the effective interest method until the debt matures and charged to the statement of comprehensive income as interest expense.

(aa) Provisions

Provisions are recognized when the Group and the Bank have a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. The assessment of provisions requires the application of management's judgment and assumptions on the probability of an outflow of resources, the probability of recovery of resources from related sources including collateral agreements and the amounts and timing of such outflows.

(bb) Dividends

Dividends are recorded in equity in the period in which they are declared. Dividends declared after the reporting date and before the financial statements are authorized for issue are disclosed in the subsequent events note. Profit distribution and other appropriations are carried out according to the Group and Bank's financial statements. The legislation of the Republic of Latvia stipulates retained earnings to be the basis of dividend payment.

3. Summary of significant accounting policies *(cont'd)*

(cc) Employee benefits

The Group and the Bank makes the State statutory social insurance contributions for state pension insurance and to the state funded pension scheme in accordance with the legislation of Latvia The State funded pension scheme is a defined contribution plan under which the Group and the Bank pay fixed contributions determined by the law and it will have no legal or constructive obligations to pay further contributions if the State pension insurance system or the State funded pension scheme is not able to settle the liabilities to employees.

Short-term employee benefits, including salaries and state statutory social insurance contributions, bonuses and paid vacation benefits, are included in administrative expenses on an accrual basis.

(dd) Off-balance sheet commitments

In the ordinary course of business, the Group and the Bank enter into off-balance sheet commitments, related to undrawn credit lines, letters of credit and financial guarantees. Financial guarantees represent irrevocable commitments to make payments in the event that a customer cannot meet its obligations to third parties and carry the same credit risk as loans. These contracts are subject to the ECL model. The provisions for off-balance sheet transactions are established in accordance with the principles described in the paragraph on provisions of Note 3(f).

(ee) Trust operations

Funds managed or held in custody by the Group and the Bank on behalf of individuals, trusts and other institutions are not regarded as assets of the Group and the Bank and, therefore, are disclosed in the off-balance sheet.

Accounting for trust operations is separated from the Group and Bank's own accounting system, thus ensuring separate accounting in a separate trust balance sheet for assets of each client, by client and by type of assets under management.

(ff) Offsetting of financial assets and liabilities

Financial assets and financial liabilities are offset and the net amount reported in the consolidated statement of financial position if, and only if, there is a currently enforceable legal right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the assets and settle the liabilities simultaneously.

(gg) Significant accounting estimates and assumptions

Fair value of financial instruments

Where the fair value of financial assets and financial liabilities, as disclosed in the statement of financial position, cannot be established using quoted market prices in an active market, the fair value is estimated using various valuation techniques, including mathematical models. The data used in such models are obtained from observable markets, if possible, in case it is not possible a certain judgment is required for determining the fair value (see also Note 3(e).

Impairment loss on financial instruments

The Group and the Bank assess their assets for impairment on a regular basis. To estimate impairment loss both in accordance with IFRS 9 and IAS 39 for all categories of financial assets, in determining the impairment loss and assessing significant increases in credit risk, the value and timing of future cash flows and collateral must be assessed (see also Note 3(b)).

3. Summary of significant accounting policies *(cont'd)*

(gg) Significant accounting estimates and assumptions *(cont'd)*

Initial recognition of related party transactions

In the ordinary course of business, the Group and the Bank perform transactions with related parties. IAS 39 requires initial recognition of financial instruments at fair value. Cases where the transactions carried out do not have an active market are subject to the management's judgment in determining interest rates on transactions and their correspondence with market interest rates. The assessment is based on similar types of transactions with unrelated parties and effective interest rate analysis.

Impairment of investments in subsidiaries (the Bank)

In the Bank's financial statements, investments in subsidiaries are stated at cost. The Bank compares the cost of the investment with the carrying amount of the subsidiary's net assets on a regular basis to ascertain whether there are no indications of impairment. If any indications of impairment are identified, the recoverable amount of the investment is calculated on the basis of the estimated future free cash flows of the subsidiary to equity. The future cash flows are based on the budgets and forecasts of the subsidiary the reliability of which is assessed. The discount rate equals the Return on equity (ROE) rate. Impairment loss is recognized when the decrease in the value of the investment in the subsidiary is substantial and sustained.

Impairment of non-financial assets

Assessment of any possible indicators of impairment of non-financial assets is done at each reporting date or more frequently if events or changes in circumstances indicate to feasible impairment of a non-financial asset. If any such indication exists, an estimate of the asset's recoverable amount is made. Where the carrying amount of an asset exceeds its recoverable amount, the asset is written down to its recoverable amount. This written down amount constitutes an impairment loss.

A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. If that is the case, the carrying amount of the asset is increased to its recoverable amount. The increase will effectively be the reversal of an impairment loss. Information on impairment assessment under IFRS 9 is presented in Note 4.

Determining the lease term of contracts with renewal and termination options – the Group and the Bank as lessees

The Group and the Bank determine the lease term as the non-cancellable term of the lease, together with any periods covered by an option to extend the lease if it is reasonably certain to be exercised, or any periods covered by an option to terminate the lease, if it is reasonably certain not to be exercised.

The Group and the Bank have several lease contracts that include extension and termination options. The Group and the Bank apply judgement in evaluating whether it is reasonably certain whether or not to exercise the option to renew or terminate the lease. That is, it considers all relevant factors that create an economic incentive for it to exercise either the renewal or termination. After the commencement date, the Group and the Bank reassess the lease term if there is a significant event or change in circumstances that is within their control and affects its ability to exercise or not to exercise the option to renew or to terminate (e.g., construction of significant leasehold improvements or significant customization to the leased asset).

The Group and the Bank included the renewal period as part of the lease term for leases of premises with shorter non-cancellable period (i.e., three to five years). The Group and the Bank typically exercise the option to renew for these leases because there will be a significant negative effect on operations if a replacement asset is not readily available. Furthermore, the periods covered by termination options are included as part of the lease term only when they are reasonably certain not to be exercised.

3. Summary of significant accounting policies *(cont'd)*

(gg) Significant accounting estimates and assumptions*(cont'd)*

Information on potential future rental payments relating to periods following the exercise date of extension and termination options that are not included in the lease term is provided in Note 4.

Leases - Estimating the incremental borrowing rate

The Group and the Bank cannot readily determine the interest rate implicit in the lease, therefore, they use their incremental borrowing rate (IBR) to measure lease liabilities. The IBR is the rate of interest that the Group and the Bank would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. The IBR therefore reflects what the Group and the Bank 'would have to pay', which requires estimation when no observable rates are available (such as for subsidiaries that do not enter into financing transactions) or when they need to be adjusted to reflect the terms and conditions of the lease (for example, when leases are not in the subsidiary's functional currency).

The Group and the Bank estimate the IBR using observable inputs (such as market interest rates) when available and are required to make certain entity-specific estimates (such as the subsidiary's stand-alone credit rating).

(hh) Adoption of new or revised standards and interpretations

The accounting policies adopted are consistent with those of the previous financial year except for the following amended IFRSs which have been adopted by the Group and the Bank as of 1 January 2019:

IFRS 16 Leases

IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, i.e. the customer ('lessee') and the supplier ('lessor'). The new standard requires lessees to recognize most leases on their financial statements. Lessees have a single accounting model for all leases, with certain exemptions. Lessor accounting is substantially unchanged. management has made an assessment of the effect of the standard and described it in Note 3(a) 'Changes in accounting policies'

IFRS 9 Prepayment features with negative compensation (Amendment)

The amendment allows financial assets with prepayment features that permit or require a party to a contract either to pay or receive reasonable compensation for the early termination of the contract (so that, from the perspective of the holder of the asset there may be 'negative compensation'), to be measured at amortized cost or at fair value through other comprehensive income. According to the management assessment, the adoption of this standard does not have a material effect on the Group and Bank's financial statements.

IAS 28: Long-term Interests in Associates and Joint Ventures (Amendments)

The amendments relate to whether the measurement, in particular impairment requirements, of long-term interests in associates and joint ventures that, in substance, form part of the 'net investment' in the associate or joint venture should be governed by IFRS 9, IAS 28 or a combination of both. The amendments clarify that an entity applies IFRS 9 Financial Instruments, before it applies IAS 28, to such long-term interests for which the equity method is not applied. In applying IFRS 9, the entity does not take account of any adjustments to the carrying amount of long- term interests that arise from applying IAS 28. According to the management assessment, the adoption of these amendments does not have a material effect on the Group and Bank's financial statements.

3. Summary of significant accounting policies *(cont'd)*

(hh) Adoption of new or revised standards and interpretations *(cont'd)*

IFRIC INTERPETATION 23: Uncertainty over Income Tax Treatments

The Interpretation addresses the accounting for income taxes when tax treatments involve uncertainty that affects the application of IAS 12. The Interpretation provides guidance on considering uncertain tax treatments separately or together, examination by tax authorities, the appropriate method to reflect uncertainty and accounting for changes in facts and circumstances. According to the management assessment, the adoption of this interpretation does not have a material effect on the Group and Bank's financial statements.

IAS 19: Plan Amendment, Curtailment or Settlement (Amendments)

The amendments require entities to use updated actuarial assumptions to determine current service cost and net interest for the remainder of the annual reporting period after a plan amendment, curtailment or settlement has occurred. The amendments also clarify how the accounting for a plan amendment, curtailment or settlement affects applying the asset ceiling requirements. These amendments are not applicable to the Group and the Bank.

The IASB has issued the Annual Improvements to IFRSs 2015 – 2017 Cycle, which is a collection of amendments to IFRSs. These amendments are not applicable to the Group and the Bank.

IFRS 3 Business Combinations and IFRS 11 Joint Arrangements: *The amendments to IFRS 3 clarify that when an entity obtains control of a business that is a joint operation, it remeasures previously held interests in that business. The amendments to IFRS 11 clarify that when an entity obtains joint control of a business that is a joint operation, the entity does not remeasure previously held interests in that business.*

IAS 12 Income Taxes: *The amendments clarify that the income tax consequences of payments on financial instruments classified as equity should be recognized according to where the past transactions or events that generated distributable profits has been recognized.*

IAS 23 Borrowing Costs: *The amendments clarify paragraph 14 of the standard that, when a qualifying asset is ready for its intended use or sale, and some of the specific borrowing related to that qualifying asset remains outstanding at that point, that borrowing is to be included in the funds that an entity borrows generally.*

Standards issued but not yet effective and not early adopted

Amendment in IFRS 10 Consolidated Financial Statements and IAS 28 Investments in Associates and Joint Ventures: Sale or Contribution of Assets between an Investor and its Associate or Joint Venture

The amendments address an acknowledged inconsistency between the requirements in IFRS 10 and those in IAS 28, in dealing with the sale or contribution of assets between an investor and its associate or joint venture. The main consequence of the amendments is that a full gain or loss is recognized when a transaction involves a business (whether it is housed in a subsidiary or not). A partial gain or loss is recognized when a transaction involves assets that do not constitute a business, even if these assets are housed in a subsidiary. In December 2015, the IASB postponed the effective date of this amendment indefinitely pending the outcome of its research project on the equity method of accounting. The amendments have not yet been endorsed by the EU.

3. Summary of significant accounting policies *(cont'd)*

(hh) Adoption of new or revised standards and interpretations *(cont'd)*

Conceptual Framework in IFRS standards

The IASB issued the revised Conceptual Framework for Financial Reporting on 29 March 2018. The Conceptual Framework sets out a comprehensive set of concepts for financial reporting, standard setting, guidance for preparers in developing consistent accounting policies and assistance to others in their efforts to understand and interpret the standards. IASB also issued a separate accompanying document, Amendments to References to the Conceptual Framework in IFRS Standards, which sets out the amendments to affected standards in order to update references to the revised Conceptual Framework. Its objective is to support transition to the revised Conceptual Framework for companies that develop accounting policies using the Conceptual Framework when no IFRS Standard applies to a particular transaction. For preparers who develop accounting policies based on the Conceptual Framework, it is effective for annual periods beginning on or after 1 January 2020.

IFRS 3: Business Combinations (Amendments)

The IASB issued amendments in Definition of a Business (Amendments to IFRS 3) aimed at resolving the difficulties that arise when an entity determines whether it has acquired a business or a group of assets. The amendments are effective for business combinations for which the acquisition date is in the first annual reporting period beginning on or after 1 January 2020 and to asset acquisitions that occur on or after the beginning of that period, with earlier application permitted. These amendments have not yet been endorsed by the EU.

IAS 1 Presentation of Financial Statements and IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors: Definition of 'material' (Amendments)

The amendments are effective for annual periods beginning on or after 1 January 2020 with earlier application permitted. The amendments clarify the definition of material and how it should be applied. The new definition states that, 'Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general-purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity'. In addition, the explanations accompanying the definition have been improved. The amendments also ensure that the definition of material is consistent across all IFRS Standards. These amendments have not yet been endorsed by the EU.

Interest Rate Benchmark Reform - IFRS 9, IAS 39 and IFRS 7 (Amendments)

The amendments are effective for annual periods beginning on or after 1 January 2020 and must be applied retrospectively. Earlier application is permitted. In September 2019, the IASB issued amendments to IFRS 9, IAS 39 and IFRS 7, which concludes phase one of its work to respond to the effects of Interbank Offered Rates (IBOR) reform on financial reporting. Phase two will focus on issues that could affect financial reporting when an existing interest rate benchmark is replaced with a risk-free interest rate (an RFR). The amendments published, deal with issues affecting financial reporting in the period before the replacement of an existing interest rate benchmark with an alternative interest rate and address the implications for specific hedge accounting requirements in IFRS 9 *Financial Instruments* and IAS 39 *Financial Instruments: Recognition and Measurement*, which require forward-looking analysis. The amendments provided temporary reliefs, applicable to all hedging relationships that are directly affected by the interest rate benchmark reform, which enable hedge accounting to continue during the period of uncertainty before the replacement of an existing interest rate benchmark with an alternative nearly risk-free interest rate. There are also amendments to IFRS 7 *Financial Instruments: Disclosures* regarding additional disclosures around uncertainty arising from the interest rate benchmark reform.

3. Summary of significant accounting policies *(cont'd)*

(hh) Adoption of new or revised standards and interpretations *(cont'd)*

IAS 1 Presentation of Financial Statements: Classification of Liabilities as Current or Non-current (Amendments)

The amendments are effective for annual reporting periods beginning on or after January 1, 2022 with earlier application permitted. The amendments aim to promote consistency in applying the requirements by helping companies determine whether, in the statement of financial position, debt and other liabilities with an uncertain settlement date should be classified as current or non-current. The amendments affect the presentation of liabilities in the statement of financial position and do not change existing requirements around measurement or timing of recognition of any asset, liability, income or expenses, nor the information that entities disclose about those items. Also, the amendments clarify the classification requirements for debt which may be settled by the company issuing own equity instruments. These amendments have not yet been endorsed by the EU.

4. Financial and other risk management

Risk management

Risk management is one of the Group and Bank's strategic tasks. Risk Management Strategy has been developed for the Group and Bank's risk management which covers management of the following risks: credit risk, operational risk, market risk, interest rate risk, foreign currency risk, liquidity risk, concentration risk, country risk, money laundering and terrorist financing risk and other risks.

For the purpose of managing these risks, internal risk management policies and procedures have been developed which are approved by the Council and/or Board of the Bank and implemented by the responsible units of the Group and the Bank.

The Board of the Bank is responsible for the development and effective functioning of the risk management system as well as ensuring the identification and management of the Bank's risks, including risk estimation, evaluation, oversight and preparation of reports through implementing the risk identification and management policy set by the Council of the Bank and other documents relating to risk management.

Risk Director is responsible for the risk control function in the Group and the Bank, oversees the risk management system and co-ordinates actions of all structural units of the Group and the Bank related to risk management. The main unit responsible for determination, evaluation and oversight of risks is the Risk management Department, which is an independent unit whose functions are separated from the functions of the business units.

The risk management system is being constantly improved in accordance with the Group and the Bank's activities and external conditions influencing these activities. The regular oversight of this process is performed by the Internal Audit Department.

(a) Credit risk

Credit risk is the risk of incurring losses in the event that a borrower (debtor) or a business partner is unable to fulfil its obligations to the Group and the Bank in accordance with the provisions of the contract. Credit risk is present in the Group and Bank's operations where the Group and the Bank make claims against another person and which are reflected in the Group and the Bank's statement of financial position and under off-balance sheet items.

The Bank's principles for evaluation, oversight and acceptance of credit risk are described and approved in its Loan Policy, Business Partner Risk Policy and Investment Portfolio Policy.

The Group and the Bank divide up and oversees their credit risk by setting limits of various types and categories: acceptable risk limits for each borrower, a group of related borrowers, geographical regions,

4. Financial and other risk management *(cont'd)*

(a) Credit risk *(cont'd)*

business sectors, type and value of collateral, currency, term and ratings granted by international agencies and other sources of possible concertation risk. Credit risk exposures are monitored on a revolving basis through regular assessments of borrowers' ability to meet interest and principal maturities and limits are adjusted as appropriate. The Group and the Bank's exposure to credit risk is managed and minimized by obtaining collaterals and guarantees against credit exposures that are registered in the name of the Bank. The fair values of both are also reviewed on a regular basis.

Credit–related commitments risks

The table below presents credit risk exposures relating to assets and off-balance sheet items:

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
Assets subject to credit risk:				
Balances on demand with the Bank of Latvia	113,348,256	113,348,256	95,088,745	95,088,745
Loans to banks	50,350,422	50,350,422	44,132,371	44,132,371
Loans to customers	54,754,717	59,297,802	85,498,479	88,260,454
Financial assets at fair value through profit or loss	31,015,724	31,015,724	25,249,486	25,249,486
Derivative financial instruments	42,340	42,340	-	-
Other financial assets	9,366,209	7,021,120	5,885,247	5,869,670
Total	**258,877,668**	**261,075,664**	**255,854,328**	**258,600,726**
Off-balance sheet items subject to credit risk:				
Contingent liabilities	5,242,483	5,242,483	6,934,513	6,934,513
Financial commitments	32,006,395	32,006,395	11,547,703	11,552,260
Total	**37,248,878**	**37,248,878**	**18,482,216**	**18,486,773**

The Group and the Bank regularly review the quality of the loan portfolio with the aim to identify loss events. In case a loss event is identified, it is assessed whether impairment should be recognized.

The Group and the Bank estimate expected credit losses (ECL), to eliminate expected present value of the cash shortfalls discounted to approximate it to ECL. Cash shortfall is the difference between the cash flows that are due to the entity in accordance with the contractual terms of a financial instrument and the cash flows that the entity expects to receive. ECL calculation techniques and key elements are provided below:

PD — Probability of default. This is an estimate of the likelihood of default over a given time horizon.

EAD — Exposure at Default. This is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date, including repayments of principal and interest, notwithstanding whether based on a contract or otherwise, and expected drawdowns on committed facilities

LGD — Loss Given Default. This is an estimate of the loss arising on default. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, including from any collateral. It is usually expressed as a percentage of the EAD.

ECL allowance is based on the estimate of losses that result from all possible default events over the period of 12 months (12m ECL), unless credit risk has increased significantly since the initial recognition of exposure, in which case the allowance is based on the risk of default over lifetime (lifetime ECL). 12-month ECLs are the portion of the lifetime ECLs that represent the ECLs resulting from default events on a financial instrument that are possible within 12 months after

4. Financial and other risk management *(cont'd)*

(a) Credit risk *(cont'd)*

Credit–related commitments risks (cont'd)

the reporting date. Both lifetime ECLs and 12-month ECLs are measured on an individual or collective basis depending on the type of underlying portfolios of financial instruments. The Bank reflects the potential future use of undrawn loan and credit card balances by applying the credit conversion factor of 75% which corresponds to the size of the currently unused facilities, which will be used over a certain period. The credit conversion factor is determined using relevant historical information and forecasts.

The Group and the Bank have established a policy for assessing at the end of each reporting period whether there has been a significant increase in credit risk since initial recognition, considering the change in the risk of default occurring over the expected life of the financial instrument.

Impairment assessment

The Group and the Bank are continuously monitoring all assets subject to ECLs. In order to determine whether an instrument or a portfolio of instruments is subject to 12mECL or lifetime ECL, the Group and the Bank assess whether there has been a significant increase in credit risk since initial recognition.

At every reporting date, the Bank assesses whether credit risk with regard to an exposure has increased significantly since initial recognition. The assessment of a significant increase in the Bank's credit risk is based on the following elements:

- quantitative element;
- qualitative element.

The main quantitative criterion is the number of days past due (hard criteria 30 days past due) and significant deterioration of the internal creditworthiness of the Customer/borrower.

Other quantitative criteria that signals about an increase in credit risk can be used, if these criteria are applicable and significant with regard to the borrower.

the Bank uses quantitative information in PD measurement models and includes it in the quantitative measurement. In cases when quantitative information cannot be included in the quantitative measurement, qualitative factors are examined individually to determine whether credit risk has increased significantly since initial recognition.

The list of indicators and indices, deterioration in which signals about an increase in credit risk, if it is applicable and topical for the borrower:

- the exposure is included on the 'List of Early Warning Signs of Deterioration in Credit Quality' of the Bank (watch list);
- amendments to the terms of contracts with the aim to improve the possibilities of debt collection, which will not reduce significantly the amount of financial commitments;
- the Bank considers the factors which might suggest potential violations of terms even if the borrower is formally observing these terms;
- overdue payments or other type of default in other banks (verification of the Credit Register data);
- assigned external rating and trends;
- other negative information regarding the key customers/counterparties/area of activity of the borrower/suppliers.

When estimating ECLs on a collective basis for a group of similar assets, the Group and the Bank apply the same principles for assessing whether there has been a significant increase in credit risk since initial recognition.

4. Financial and other risk management *(cont'd)*

(a) Credit risk *(cont'd)*

Grouping financial assets measured on a collective basis

Dependent on the factors below, the Group and the Bank calculate ECLs either on a collective or on an individual basis. Asset classes where the Group and the Bank calculate ECL on an individual basis include:

- All Stage 3 assets which exceed the materiality threshold (i.e. the balance of exposure exceeds EUR 1 million) defaulted prior to 2018, regardless of the class of financial assets;
- Due from other banks.

Asset classes where the Group and the Bank calculate ECL on a collective basis include:

- All Stage 1 and 2 assets.
- Stage 3 assets defaulted in 2018, which do not exceed the materiality threshold (EUR 1 million), are assessed within a group.

Under the above procedure, the Group and the Bank organize their loans as Stage 1, Stage 2 and Stage 3 as described below:

Stage 1: Upon initial recognition of a loan, the Group and the Bank recognize loss allowance based on 12 -month ECLs. Stage 1 can also include exposures moved from Stage 2 if seeing decrease of the respective credit risk.

Stage 2: Assets with significant increase in credit risk since initial recognition. For these assets the Group and the Bank recognize loss allowance based on lifetime ECL. Stage 2 can also include exposures moved from Stage 3 if seeing decrease of the respective credit risk.

Stage 3: Financial assets that have objective evidence of impairment at the reporting date. For these assets the Group and the Bank recognize loss allowance based on lifetime ECL.

Definitions of default and cure

The Group and the Bank consider a financial instrument in default and, accordingly Stage 3 (credit-impaired financial asset) for ECL calculations, when contractual payments are 90 days past due. The Group and the Bank consider the amounts due from banks in default and act, without delay, if the demanded daily payments are not settled by the end of the business day as specified in individual contracts.

In performing a qualitative assessment as to whether a customer complies with their obligations, the Group and the Bank also consider various events that can indicate an inability to pay (default events). In such cases, the Group and the Bank carefully consider whether it can be deemed that the customer does not comply with their obligations and whether the respective exposure should be classified in Stage 3 or Stage 2. Such events are:

- Internal rating of the borrower indicating default or partial default;
- A borrower asks an emergency funding from the Group and the Bank;
- Significant decrease in the value of underlying collateral if recovery of the loan is expected from collateral;
- Significant decrease in the borrower's turnover or loss of their key customer;
- Breach of the contractual terms not repudiated by the Group and the Bank;
- Debtor (or any legal entity of the debtor's group) files for bankruptcy;
- Debtor's listed debt or equity suspended at the primary exchange because of rumors or facts about financial difficulties.

The policy of the Group and the Bank is to consider a financial instrument as 'cured' (it no longer meets any of the default criteria) and, accordingly, to move it from Stage 3 if any of the default criteria other than restructuring has not been in force at least for a consecutive period of 12 months to be reclassified to Stage 2, and at least 24 months to be reclassified from Stage 3 to Stage 1. A decision on whether the cured asset should be classified as Stage 1 or Stage 2 asset depends on the updated credit category over the cure period and whether it indicates a significant increase in credit risk in comparison with initial recognition.

4. Financial and other risk management *(cont'd)*

(a) Credit risk *(cont'd)*

Internal rating and PD estimation

The number of days past due is used as the principal indicator for calculation of PD and internal credit rating for calculation of provisions. The PD rate is calculated for each of the following groups of delay:

- not past due;
- increased credit risk;
- past due for 1-30 days;
- past due for 31-60 days;
- past due for 61-90 days;
- forborne not past due;
- forborne past due 1-30 days;
- non-performing exposures.

PD rates are calculated using Markov's transmission matrices (TM) which reflect the movement of the lending portfolio between the groups of delays within one month. The transfer to another category is determined by using the number of migrations of loans. The calculation is based on TM data for 36 months before the end of the reporting period.

Exposure at default

An exposure at default (EAD) equals to the gross carrying amount of the financial instruments subject to impairment assessment and it refers both to the customer's ability to increase risk, while approximating a default event, and the potential early repayment. In order to measure EAD for Stage 1 exposure, the Group and the Bank assess the possible defaults over 12 months to calculate 12mECL. For Stage 2 , Stage 3, in case of default, events over the lifetime of the respective instruments are considered.

Exposure at default (cont'd)

The Group and the Bank determine EAD, by modeling the range of possible outcomes over various horizons in several scenarios. Subsequently, PD, as defined in IFRS 9, is assigned to each economic scenario on the basis of the outcomes of the model used by the Group and the Bank.

Loss given default

The Bank and the Group assess the LGD values and the Bank's Asset and Liability Committee reviews and approves thereof at least quarterly as well as whenever the Bank becomes aware of information indicating significant deterioration in the quality of an asset or contingent liability.

The credit risk assessment is based on a standardized LGD assessment approach as a result of which a certain LGD rate is obtained. Such LGD rates consider the expected EAD in comparison with the amount expected to be recovered or obtained from collateral.

Forward- looking information

In calculating ECL, the Group and the Bank consider if adjustments are needed in respect to the relevant forward-looking information. The Group and the Bank obtain forward-looking information from reliable third-party sources (such as external rating agencies, governmental bodies and international financial institutions). The Group and the Bank assess:

- every sector of economy, in which the Bank has significant credit risk exposures;
- macroeconomic data at a national level in every region, in which the Bank has significant credit risk exposures;
- relevant trends on real estate market;
- other relevant information.

Notes to the financial statements *(cont'd)*

4. Financial and other risk management *(cont'd)*

(a) Credit risk *(cont'd)*

When the Bank identifies relevant correlations with available macro-economic data, it uses these correlations to adjust relevant inputs and estimates used in the expected credit losses calculation. As at the end of 2019 no such correlations were identified.

In estimating the ECL, the Bank considers several potential scenarios. The Bank determines base scenario ECL; the base scenario in this case means LGD calculated considering recoveries from date of default to derecognition of relevant exposures and PD calculated considering 3 years historical migration data. Once a year (usually at the end of the financial year), two more additional scenarios are determined and calculated:

- determining the base scenario LGD and PD calculated based on 4 years historical data;
- determining LGD considering recoveries during the most recent 5 years historical data and base scenario PD.

An average ECL of the base scenario and the two additional scenarios is calculated. Where the ECL amount under the base scenario exceeds the average of the three scenarios, the ECL result of the base scenario is not adjusted; where the average results of the three scenarios ECL exceed the base scenario ECL, the Bank uses the average ECL amounts for calculating the ECL allowances.

The table below presents the ECL sensitivity of PD and LGD fluctuations at the end of the reporting period, with all other variables held constant (in thousand EUR):

4YPD	Effect on ECL	5YLGD	Effect on ECL
	(460)		(1022)
Total	**(460)**	**Total**	**(1022)**

The table below presents the ECL sensitivity of Stage 3 loans depending on collateral, if the price increases or drops at the end of the reporting period, with all other variables held constant (in thousand EUR):

31.12.2019	Effect on ECL	
	+10%	-10%
ECL	(340)	220
Total	**(340)**	**220**

(b) Market risk

The Group and the Bank are exposed to market risks which arise from open positions in interest rate and currency, all of which are exposed to general and specific market movements.

The Group and the Bank manage market risks by diversifying the financial instruments portfolio, setting limits on different types of financial instruments and applying sensitivity tests which show the impact of particular risks on the Group and Bank's assets and equity.

Basis of the market risk management:

- Assessment and analysis of securities portfolio;
- Analysis and monitoring of issuers' financial position;
- Establishing internal limits/ diversification (stop-loss to issuers, countries, regions, terms, credit rating categories);
- Monitoring of the compliance of the internal limits.

4. Financial and other risk management *(cont'd)*

(c) Currency risk

The Group and the Bank are exposed to the risk of changing foreign currency exchange rates which impacts both the financial performance and the cash flows of the Group and the Bank. The Group and the Bank control assets and liabilities denominated in foreign currencies to avoid unreasonable foreign currency exchange rate risk. Currency risk is calculated for each currency separately taking into account the amount of liabilities and requirements of the Group and the Bank. The Board determines the Group and Bank's open position limits on certain currencies which are monitored daily. The Latvian banking legislation requires that open positions in each foreign currency may not exceed 10% of the Group and Bank's equity and that the total foreign currency open position may not exceed 20% of the equity. In 2019 and 2018 the Group and the Bank complied with these limits (see Note 29). The Group and the Bank have no significant open positions in 'exotic' currencies.

The Group and Bank's foreign currency risk assessment is based on the following main principles:
- Assessment is made of changes in the Group and Bank's assets, liabilities and off-balance sheet items as a result of exchange rate fluctuations;
- How the Group and Bank's revenue/costs change with exchange rate fluctuations;
- Performing currency risk stress tests.

Basis of the currency risk management:
- Assessing currency risk;
- Setting of limits and restrictions;
- Monitoring of adherence to internal limits;
- Performing exchange rate stress tests and analyzing the obtained results;
- Entering into hedge relationships, if necessary.

The Group and the Bank define and control daily and weekly maximum loss limits via involving in currency trading.

As part of a quarterly currency risk management process, assessment of the foreign exchange risk is performed (assessment how the statement of financial position and off-balance sheet items change with the changes in foreign currency exchange rates, how the income/expenses of the Group and the Bank change with the foreign currency exchange rate changes) and the results of such evaluation are submitted to the management of the Group and the Bank. Once a year a currency risk stress testing and the analysis of its results are performed, serving as the basis of proposals for changes in the foreign currency risk management policy which are made to the management of the Group and the Bank, if necessary.

The table below presents the sensitivity of profit/ loss to currency exchange rate fluctuations at the end of the reporting period with all other variables held constant (in thousand EUR):

31.12.2019	Effect on net profit/ loss and equity		31.12.2018	Effect on net profit/ loss and equity	
	+10%	-10%		+10%	-10%
USD	(55)	55	USD	40	(40)
Total	**(55)**	**55**	**Total**	**40**	**(40)**

(d) Interest rate risk

Interest rate risk is the sensitivity of the Group and Bank's financial position to a change in market interest rates. In the normal course of business, the Group and the Bank encounter interest rate risk as a result of differences within maturities or interest re-fixing dates of respective interest-sensitive assets and liabilities. The risk is controlled by the Bank's Asset and Liability Committee which sets limits on the level of mismatch of interest rate reprising and evaluates interest rate risk undertaken by the Group and the Bank (see Note 31).

4. Financial and other risk management *(cont'd)*

(d) Interest rate risk *(cont'd)*

Basis of the interest rate management:

- Assessing sensitivity of interest rate risk;
- Setting of internal limits (limit of reduction in economic value and for total duration of securities portfolio);
- Monitoring of adherence to internal limits;
- Performing interest rate stress tests and analyzing the obtained results;
- Entering into hedge relationships, if necessary.

Interest rate risk identification and assessment are made in a way as to further examine all types of interest-rate risks. To limit the interest rate risk, limits are set to both impairment of economic value and the modified duration of securities portfolio.

As part of interest rate risk assessment, impact of interest rate changes on the economic value of the Group and the Bank is performed regularly, including interest rate risk assessment from income perspective and interest rate risk assessment from the perspective of economic value, and on that basis, follow up control of the set limits is carried out. Moreover, interest rate risk stress testing is performed, based on which changes are proposed in the interest rate risk management policies, if needed. Results of interest rate risk assessment are reported to the management of the Group and the Bank.

Assets/ liabilities/ off-balance sheet items with specified maturity are split into maturity groups as follows:

- Shorter from the remaining repayment/ settlement/ maturity term – for financial instruments with fixed interest rate;
- For a period until the next interest rate change date or interest repricing date – for financial instruments with variable interest rate;
- Maturity of deposits is shown as being not longer than five years.

Assets/ liabilities/ off-balance sheet items with no specified maturity are split into maturity groups as follows:

- Settlement accounts, for which interest is paid, are classified as sensitive to the changes in interest rates and presented as 'on demand';
- Derivatives are presented under both long off-balance-sheet position and short off-balance-sheet position.

The following changes in interest rates are applied to the sensitivity analysis: all items except for deposits are subject to rate changes of +/-100 base points, while deposits are subject to rate changes of +/-50 base points.

The table below presents the sensitivity of revenue and equity to interest rate fluctuations as described above with all other variables held constant (in thousand EUR):

31.12.2019	Effect on net profit/ loss and equity		31.12.2018	Effect on net profit/ loss and equity	
USD	(117)	117	USD	(143)	143
EUR	65	(65)	EUR	(194)	194
Total	**(52)**	**52**	**Total**	**(337)**	**337**

(e) Liquidity risk

The Group and the Bank are exposed to daily calls on its available cash resources from short-term liquid investments. The relationship between the maturity of assets and liabilities, as well as off-balance sheet items, is indicative of liquidity risk and the extent to which it may be necessary to raise funds to meet outstanding obligations.

The Group and the Bank do not maintain cash resources to meet all of these needs, as experience shows that a minimum level of reinvestment of maturing funds can be predicted with a high level of certainty.

4. Financial and other risk management *(cont'd)*

(e) Liquidity risk *(cont'd)*

The Board sets limits on the minimum proportion of maturing funds available to meet such calls and at the minimum level of inter-bank and other borrowing facilities that should be in place to cover withdrawals at unexpected levels of demand.

It is unusual for banks to be completely matched, as transacted business is often of uncertain term and of different types (see Note 30). An unmatched position potentially enhances profitability, but also increases the risk of losses.

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature are important factors in assessing the liquidity of the Group and the Bank and their exposure to changes in interest rates and exchange rates.

The matching and controlled mismatching of the maturities of assets and liabilities are fundamental to the daily liquidity management of the Group and the Bank.

The Group and the Bank use the following methods for evaluation of liquidity risk:

- Preparation of maturity analysis (for all currencies and separately for individual currencies);
- Calculation of the liquidity ratio, monitoring of adherence to liquidity ratio regulations;
- Stress testing.

Basis of the liquidity risk management:

- Being in compliance with liquidity ratio regulations;
- Setting of the liquidity net position limit;
- Setting of restriction on attracting deposits;
- Monitoring of adherence to liquidity limits;
- Conducting liquidity stress tests and analysis of the obtained results;
- Recommendations for resolving liquidity problems.

In accordance with the FCMC requirements, the Bank maintains sufficient liquid assets to meet its liabilities in the amount which is not less than 60% of the Bank's current liabilities.

(f) Capital adequacy

Capital adequacy refers to the sufficiency of the Group and Bank's own funds to cover risks resulting from the Group and Bank's operating activities. In order to calculate the capital for risks to which minimal capital requirements are set, according to the Financial and Capital Market Commission's (FCMC) regulations on preparation of report on minimal capital requirements, capital requirements are calculated using the following approaches and methods:

- Credit risk capital requirements are calculated using the standardized approach;
- The Financial Collateral Simple Method is used in order to decrease credit risk;
- The Bank calculates the portfolio own funds requirements for CVA risk applying the standardized method specified in Article 384 of EU Regulation No 575/2013;
- Foreign currency risk capital requirements, commodities risk capital requirements and capital requirements for position risk of debt securities and equities are calculated using the standardized approach;
- Capital requirements for general risk of debt securities are calculated using the maturity method;
- Capital requirements for operational risk are calculated using the basic index approach.

The Group and the Bank also evaluate whether compliance with the minimal capital requirements ensures that the capital of the Group and the Bank is sufficient to cover all possible losses associated with all of the above mentioned risks).

Moreover, the Group and the Bank have developed internal documentation and regulations according to which they determine the amount of necessary capital for substantial risks to which minimal capital requirements are not set (e.g., interest rates risk, liquidity risk, country risk, and other substantial risks).

4. Financial and other risk management *(cont'd)*

(f) Capital adequacy *(cont'd)*

Calculated in accordance with the FCMC requirements, the Group and Bank's capital adequacy ratio as at 31 December 2019 was 27,58% and 26,95% (31 December 2018: 26.96% and 27.21%), which is above the minimum set by European Parliament and the Council Regulation (EU) No 575/2013 requiring capital

retention reserve amount (10.5%), being a sum of equity against risk weighted assets and off-balance sheet items being minimum of 8% and capital retention reserve above 2.5% (see Note 28). On 26 February 2019, the Financial and Capital Market Commission recalculated the capital adequacy requirement applicable both individually to the Bank and collectively at the Group level and assessed it at 11.90%. The Group and the Bank observed and complied with the individually determined capital adequacy requirements in 2019.

(g) Operational risk

Operational risk is the possibility of incurring losses as a result of inadequate or unsuccessful developments in the Group and Bank's internal processes, human and systemic actions, or influence of external conditions. Operational risk is defined as the risk of a reduction in the Group and Bank's revenue/ incurring of additional costs (and a resulting reduction of the equity) due to erroneous transactions with customers/business partners, information processing, adoption of ineffective decisions, insufficient human resources or insufficient planning for the influence of external conditions.

The Group and the Bank have established and maintain an Operational Risk Event and Loss database in which internal data on operational risk events and associated losses are collected, processed and organized.

Basis of the operational risk management:

- Monitoring of operational risk;
- management and minimizing of operational risk:
- Development of internal regulations which eliminate/ reduce the possibility of operational risk events;
- Compliance with the principle of separation of duties;
- Monitoring of compliance with the internal limits;
- Compliance with the procedure for using IT and other resources of the Bank;
- Adequate staff training;
- Review of transactions and account documentation on a regular basis.

(h) Concentration risk

Transaction concentration risk

Transaction concentration risk is any risk transaction or group of risk transactions that could cause the Group and the Bank to suffer such losses that may endanger the liquidity of the Group and the Bank or their ability to continue as a going concern. Concentration risk arises from significant risk transactions with customers or groups of inter-related customers or risk transactions with customers with common risk factors (e.g., economy sector, geographical region, currency, the instrument used for decreasing credit risk (one type of collateral or one provider of collateral, etc.)).

In order to control transaction concentration risk the Group and the Bank have set limits on investments into various types of assets, instruments, markets, etc. Limit is a numerical threshold applied to various types of investments serving as an instrument for limiting and controlling the risk.

4. Financial and other risk management *(cont'd)*

(h) Concentration risk *(cont'd)*

Country risk

Country risk is one of significant transaction concentration risks. Country risk – country partner risk – is the possibility of incurring losses if the Group and Bank's assets are located in a country where, due to changes in its economic and political factors, the Group and the Bank may experience problems in recovering its assets within the agreed time and amount. The reasons of default by partners and issuers are primarily currency devaluation, unfavorable legislative changes, creation of new restrictions and barriers as well as other, including force majeure, factors.
In order to manage concentration risks the following limits were set:

- Country risk limits;
- Credit rating group limits;
- Financial market operations risk limits;
- Limits on open currency positions and cash, limits on allowable loss on trading with foreign currencies;
- Limits on allowable loss from trading with financial instruments portfolios;
- Limits on large exposures;
- Limits on transactions with parent bank;
- Limits on lending programs.

Control, analysis and review of fulfilment of these limits are performed.

Basis of the risk management:

- Setting of internal limits by regions, countries, and by transaction types in individual countries;
- Monitoring of adherence to internal limits;
- Analysis and monitoring of country risk;
- Review of internal limits.

Asset, liability and off-balance sheet country risk applies to the country which is considered to be the primary country where the customer conducts its business activities. If a loan is granted to a resident of another country using collateral which is physically located in a country other than the resident country of the legal entity, the country risk is transferred to the country where the loan collateral is actually located.

International rating agency data (including credit ratings and their dynamics), economic indicators of the country and other relevant information sources are used for country risk analysis.

The table below reflects composite ratings of Latvia, TOP3 OECD countries, and TOP3 non-OECD countries.

TOP countries have been selected taking into account the volume of transferred exposures.

Latvia – Composite rating (Moody's/ Fitch un S&P)		OECD – Composite rating (Moody's/ Fitch un S&P)		Non-OECD 0150 Composite rating (Moody's/ Fitch un S&P)	
Country	Rating	Country	Rating	Country	Rating
Latvia	A3/A-	ASV	Aaa/AAA	Ukraine	B2/B
-	-	Luxemburg	Aaa/AAA	Russia	Baa3/BBB-
-	-	Austria	Aa1/AA+	China	A1/A+

4. Financial and other risk management *(cont'd)*

(h) Concentration risk *(cont'd)*

The table below reflects the breakdown of assets and liabilities by groups of countries.

	Latvia		OECD		Non-OECD		31.12.2019	31.12.2019
	Group	Bank	Group	Bank	Group	Bank	Group	Bank
	EUR	EUR	EUR	EUR	EUR	EUR	EUR	EUR
Financial assets								
Cash and balances with the Bank of Latvia	113,348,256	113,348,256	-	-	-	-	113,348,256	113,348,256
Balances due from banks	71	71	28,138,850	28,138,850	22,211,501	22,211,501	50,350,422	50,350,422
Loans and advances to customers	11,111,361	15,654,446	15,762,766	15,762,766	27,880,590	27,880,590	54,754,717	59,297,802
Financial assets at fair value through profit or loss	1,216,687	1,216,687	29,610,939	29,610,939	188,098	188,098	31,015,724	31,015,724
Equity instruments at fair value through other comprehensive income	-	-	412,205	412,205	-	-	412,205	412,205
Derivative financial instruments	-	-	42,340	42,340	-	-	42,340	42,340
Other financial assets	108,287	108,287	9,234,041	6,888,951	4,901	4,901	9,347,229	7,002,139
Total assets	**125,784,662**	**130,327,747**	**83,201,141**	**80,856,051**	**50,285,090**	**50,285,090**	**259,270,893**	**261,468,888**

	Latvia		OECD		Non-OECD		31.12.2019	31.12.2019
	Group	Bank	Group	Bank	Group	Bank	Group	Bank
	EUR	EUR	EUR	EUR	EUR	EUR	EUR	EUR
Liabilities								
Deposits from customers	45,994,255	46,448,378	82,048,140	82,048,140	93,916,658	93,916,658	221,959,053	222,413,176
Other financial liabilities	1,848,501	847,718	204,285	10,399	-	-	2,052,786	858,117
Deferred income and accrued expense	938,238	938,238	9,174	9,174	19,291	19,291	966,703	966,703
Debt securities	-	-	17,017,479	17,017,479	878,941	878,941	17,896,420	17,896,420
Subordinated loans	-	-	5,706,141	5,706,141	3,042,506	3,042,506	8,748,647	8,748,647
Total liabilities	**48,780,994**	**48,234,334**	**104,985,219**	**104,791,333**	**97,857,396**	**97,857,396**	**251,623,609**	**250,883,063**

4. Financial and other risk management *(cont'd)*

(h) Concentration risk *(cont'd)*

The table below reflects the breakdown of assets and liabilities by groups of countries.

	Latvia		OECD		Non-OECD		31.12.2018	31.12.2018
	Group	Bank	Group	Bank	Group	Bank	Group	Bank
	EUR	EUR	EUR	EUR	EUR	EUR	EUR	EUR
Financial assets								
Cash and balances with the Bank of Latvia	95,088,745	95,088,745	-	-	-	-	95,088,745	95,088,745
Balances due from banks	688	688	21,908,739	21,908,739	22,222,944	22,222,944	44,132,371	44,132,371
Loans and advances to customers	19,134,227	21,896,202	17,572,917	17,572,917	48,791,335	48,791,335	85,498,479	88,260,454
Financial assets at fair value through profit or loss	1,273,368	1,273,368	23,443,610	23,443,610	532,508	532,508	25,249,486	25,249,486
Equity instruments at fair value through other comprehensive income	-	-	284,083	284,083	-	-	284,083	284,083
Other financial assets	1,147,633	1,147,633	4,653,398	4,637,821	84,216	84,216	5,885,247	5,869,670
Total assets	**116,644,661**	**119,406,636**	**67,862,747**	**67,847,170**	**71,631,003**	**71,631,003**	**256,138,411**	**258,884,809**

	Latvia		OECD		Non-OECD		31.12.2018	31.12.2018
	Group	Bank	Group	Bank	Group	Bank	Group	Bank
	EUR	EUR	EUR	EUR	EUR	EUR	EUR	EUR
Liabilities								
Deposits from customers	51,069,820	51,077,003	57,391,149	57,391,149	109,369,474	109,369,474	217,830,443	217,837,626
Other financial liabilities	2,824,170	2,824,170	53,458	28,862	54,576	54,576	2,932,204	2,907,608
Deferred income and accrued expense	916,982	916,982	16,254	16,254	48	48	933,284	933,284
Debt securities	-	-	16,784,496	16,784,496	774,314	774,314	17,558,810	17,558,810
Subordinated loans	366,899	366,899	370,562	370,562	10,469,896	10,469,896	11,207,357	11,207,357
Total liabilities	**55,177,871**	**55,185,054**	**74,615,919**	**74,591,323**	**120,668,308**	**120,668,308**	**250,462,098**	**250,444,685**

4. Financial and other risk management *(cont'd)*

(i) Money laundering and terrorist financing risk

The main policies and procedures as well as control mechanisms of the Group and the Bank in the area of the anti-money laundering and terrorist financing are based on the following documents:

- Laws and regulations of the Republic of Latvia and European Union in the area of anti-money laundering and terrorist and proliferation financing;
- FATF (Financial Action Task Force) recommendations;
- Wolfsberg standards;
- Basel Committee Principles, etc.

The Group and Bank's internal regulations include the following programs:

- Money Laundering and Terrorist Financing Risk Management Strategy 2019 – 2021;
- Sanctions risk management policy;
- Program for customer identification and examination and for determination and identification of ultimate beneficial owner;
- Program for mandatory monitoring of customer operations and identification of suspicious transactions and activities;
- Program for customer information verification;
- Program for documenting the necessary information
- Program for information and documentation maintenance;
- Program for the training of the Bank's employees in the areas of AML/CFT and sanctions;
- Program setting forth limits for cash transactions and transactions with other assets;
- Program for threshold declarations and suspicious transaction reporting.

When meeting the above mentioned regulatory requirements and implementing the policies 'Know Your Customer' and 'Know Your Customers' Partners', the Bank performs customer and transaction party due diligence during which it:

- Identifies and verifies ultimate beneficial owners;
- Obtains information on the nature of the intended cooperation;
- Obtains information on the customer's business or personal life as well as about the origin of funds;
- Establishes the customer ML/FT risk category;
- Establishes the customer sanctions risk category;
- Obtains information on the ultimate beneficial owner;
- Obtains information on the objective of the transaction and its expected nature;
- Monitors transactions and obtains information and documents supporting the account transactions;
- Ensures security of the documentations, data and information obtained during the customer investigation as well as updates it on a regular basis.
-

A more detailed description of the money laundering and terrorist and proliferation financing risk management is provided in the Policy for the Prevention of Money Laundering and Terrorist Financing as well as in the Group and Bank's instructions.

The Bank continuously improves its internal regulatory framework, following the amendments in regulatory enactments in the areas of AML/CFT and sanctions applications in 2019.

According to FCMC Regulation No.13 'Regulations on sanctions risk management', the Bank, in its procedures, has established and implemented both the Bank's general assessment of sanctions risk and individual scoring of each customer regarding sanctions risk.

4. Financial and other risk management *(cont'd)*

Money laundering and terrorist financing risk *(cont'd)*

With coming into effect of FCMC Regulation No.135 'Regulations on the Establishment of Customer Due Diligence, Enhanced Customer Due Diligence and Risk Scoring System', the Bank established new processes and considerably modified the existing processes:

- A new customer scoring model was established, stipulating incorporation of the mandatory factors which trigger immediate enhanced customer due diligence and factors that can be identified during the due diligence which trigger enhanced due diligence of the customer's purposes,
- A new process for timely identification of the new ML/TF risk factors was established;
- Internal procedures have been improved in the areas of enhanced customer due diligence and monitoring and quantification of customer ML/TF and sanctions risk.

As of 17 December 2019, according to the last amendments to the AML/CFT Law, the Bank has introduced a new process – filing threshold declarations with the Financial Intelligence Unit while terminating unusual transaction reporting.

The Bank has reviewed and updated its Money Laundering and Terrorist Financing Risk Management Strategy 2019-2021, which aims to develop ML/TF risk management culture at the Bank, maintain good reputation of the Bank, establish the limits of the Bank's ML/TF risk exposures and the core principles and methods for the ML/TF risk management while ensuring a clear and understandable ML/TF risk management framework.

The Bank has implemented the requirements of AML/CFTP in the Bank's AML/CFTP procedures, instructions and thematic methodologies, where additional criteria such as obtaining and analyzing of the financial statements, tax returns and annual income statements are considered in the enhanced due diligence process.

The Bank continues ongoing improvement of IT systems ensuring automated AML/TPF risk and sanctions risk management processes (processing and managing customer information; determining ML/TF and sanction risk scores; sanction screening, etc.).

The Bank continuously invests in developing an effective AML/TPF risk management and internal control system and its ongoing improvement – enhancing the staff competence and system improvement, which allows the Bank to assume and manage the risks inherent to it.

5. Interest income and expense

	2019 Group EUR	2019 Bank EUR	2018 Group EUR	2018 Bank EUR
Interest income				
Loans and advances to legal entities	5,961,255	6,119,449	6,336,507	6,443,282
Loans and advances to private individuals	510,341	510,341	789,894	789,894
Balances due from banks	598,775	598,775	1,311,174	1,311,174
Debt securities held for trading	505,574	505,574	624,119	624,119
Other interest income	-	-	20,438	20,438
Total interest income	**7,575,945**	**7,734,139**	**9,082,132**	**9,188,907**
Interest expense				
Due to private individuals	(142,208)	(142,208)	(64,996)	(64,996)
Due to legal entities	(240,022)	(240,022)	(1,058,098)	(1,058,098)
Subordinated loans	(846,400)	(846,400)	(998,741)	(998,741)
Debt securities issued	(803,970)	(803,970)	(762,614)	(762,614)
Other interest and related expense	(710,877)	(710,877)	(624,418)	(624,418)
Interest expense on lease liabilities (see also Note 17)	(3,620)	(3,620)	-	-
Total interest expense	**(2,747,097)**	**(2,747,097)**	**(3,508,867)**	**(3,508,867)**
Net interest income	**4,828,848**	**4,987,042**	**5,573,265**	**5,680,040**

Other interest and related expense include payments to the deposit guarantee fund of EUR 131,288 (2018: EUR 149,048), which are calculated in accordance with the Deposit Guarantee Law and FCMC regulations 'Regulations for preparing a report of guaranteed deposits and for determining the adjustment ratio to be applied to the payments in the deposit guarantee fund'; as well as financial stability fee of EUR 113,932 (2018: EUR 43,855); negative interest rate applied to correspondent accounts of EUR 395,717 (2018: EUR 431,515) and deposit referral fee of EUR 69,940 (2018: 0 EUR)

6. Fee and commission income and expense

	2019 Group EUR	2019 Bank EUR	2018 Group EUR	2018 Bank EUR
Fee and commission income				
Money transfers	835,876	836,089	1,769,745	1,770,031
Fees on registration of changes in loan agreements	5,027	5,027	4,315	4,315
Commission income on asset management	636,230	636,230	510,375	510,375
Account servicing	1,969,553	1,969,553	2,575,193	2,575,193
Commissions on letters of credit	205,193	205,193	428,467	428,467
Commission income on transactions with securities	67,780	67,780	91,493	91,493
Commission income on current accounts servicing	2,178	2,178	5,405	5,405
Income from general services	69,203	69,203	71,478	71,478
Other commissions (DIGIPAS)	12,398	12,398	34,271	34,271
Interbank commission income	133,604	133,604	239,910	239,910
Commission on transactions with settlement cards	251,117	251,117	656,926	656,926
Income from currency exchange	1,477	1,477	292	292
Other income	7,821	7,821	16,482	16,482
Total fee and commission income	**4,197,457**	**4,197,670**	**6,404,352**	**6,404,638**
Fee and commission expense:				
Money transfers	(402,585)	(402,480)	(768,908)	(768,798)
Other expense	(52,649)	(52,649)	(20,649)	(20,649)
Total fee and commission expense	**(455,234)**	**(455,129)**	**(789,557)**	**(789,447)**
Net fee and commission income	**3,742,223**	**3,742,541**	**5,614,795**	**5,615,191**

Notes to the financial statements *(cont'd)*

7. Administrative expense

	2019 Group EUR	2019 Bank EUR	2018 Group EUR	2018 Bank EUR
Remuneration paid to personnel	(3,894,320)	(3,894,320)	(4,189,453)	(4,189,453)
State statutory social insurance contributions	(1,162,072)	(1,160,829)	(1,198,426)	(1,196,400)
Remuneration paid to the Members of the Council and the Board	(802,051)	(796,891)	(618,631)	(610,220)
Communications expense	(460,770)	(460,770)	(519,350)	(519,350)
Set-up and maintenance costs of information systems	(280,182)	(280,182)	(258,005)	(258,005)
Fee paid to the certified auditor *	(239,240)	(239,240)	(111,010)	(111,010)
Non-deductible VAT	(135,729)	(135,729)	(153,601)	(153,601)
Consulting and professional fees	(194,359)	(131,568)	(262,385)	(196,528)
Public utilities	(89,739)	(89,739)	(96,348)	(96,348)
Real estate tax	(98,534)	(84,761)	(67,399)	(67,399)
Business trips	(61,309)	(57,056)	(74,766)	(74,053)
Health insurance	(38,336)	(38,336)	(36,045)	(36,045)
Postal charges	(28,173)	(28,173)	(38,349)	(38,349)
Office and equipment maintenance	(26,416)	(26,416)	(20,279)	(20,279)
Stationary	(19,172)	(19,172)	(19,400)	(19,400)
Advertising and marketing	(7,641)	(7,641)	(12,037)	(12,037)
Operating lease expense	-	-	(28,361)	(28,361)
Expense related to short-term leases (see also Note 17)	(9,297)	(9,297)	-	-
Transport expense	(5,839)	(5,839)	(10,801)	(10,801)
Security	(1,202)	(1,202)	(1,487)	(1,487)
Other administrative expense	(259,870)	(227,323)	(181,276)	(151,896)
Total administrative expense	**(7,814,251)**	**(7,694,484)**	**(7,897,409)**	**(7,791,022)**

The average number of staff employed by the Group and the Bank in 2019 was 159, including 4 Members of the Board, 5 Members of the Council and 150 other employees (2018: 191, including 4 members of the Board, 5 Members of the Council and 182 other employees). The remuneration paid to the Members of the Council and the Board is disclosed in Note 32.

* The total fee paid to the certified auditor for the types of services provided by the auditor was as follows: statutory annual audit of consolidated and separate financial statements – EUR 216,140 (2018: EUR 82,810), other audit tasks - EUR 6,000 (2018: EUR 7,500); to other specialists – EUR 17,100 (2018: EUR 20,700).

8. Other operating income

	2019 Group EUR	2019 Bank EUR	2018 Group EUR	2018 Bank EUR
Rentals	319,662	284,142	209,533	167,773
Penalties	109,957	109,957	381,500	381,500
Other income	848,425	10,781	146,772	35,222
Total other operating income	**1,278,044**	**404,880**	**737,805**	**584,495**

Increase in the Group's income in 2019, compared to 2018, is related to the one-time contractual penalty received by the Bank's subsidiary company for freeing the collateral deposit.

9. Other expense

	2019 Group EUR	2019 Bank EUR	2018 Group EUR	2018 Bank EUR
Payments to funds and membership fees	(253,915)	(253,915)	(296,799)	(296,799)
Loss on loan realization, net	-	-	(214,581)	(214,581)
Loss on disposal of repossessed collateral, net	-	-	(387,002)	(387,002)
Other expense	-	-	(13,807)	-
Penalties	(1,348)	(1,348)	(894)	(894)
Total other expense	**(255,263)**	**(255,263)**	**(913,083)**	**(899,276)**

10. Corporate income tax

	2019 Group EUR	2019 Bank EUR	2018 Group EUR	2018 Bank EUR
Corporate income tax for the reporting year	(7,531)	(7,531)	(2,098)	(2,098)
*Amount of tax paid abroad	(141,990)	(141,990)	(214,423)	(214,423)
Change in deferred corporate income tax (see also Note 25)	-	-	-	-
Total corporate income tax	**(149,521)**	**(149,521)**	**(216,521)**	**(216,521)**

* The amount of tax paid abroad consists of withholding tax paid in Ukraine. Corporate income tax from dividends calculated in Latvia can be reduced by the amount of tax paid abroad, if the payment is certified by the documents approved by a foreign tax authority, stating the amount of taxable income and the amount of tax withheld abroad. Tax can be reduced by the amount of tax withheld abroad, however, limited to the amount, which would be payable in Latvia for the amount of revenue generated abroad. Amounts of withholding tax, exceeding the tax calculated in Latvia, cannot be carried forward to the future periods, therefore, are recognized as tax expense in the current period.

11. Cash and balances with the Bank of Latvia

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
Cash	729,668	729,668	925,139	925,139
Balances on demand with the Bank of Latvia	112,629,851	112,629,851	94,173,023	94,173,023
ECL allowances	(11,263)	(11,263)	(9,417)	(9,417)
	113,348,256	**113,348,256**	**95,088,745**	**95,088,745**

Balances on demand with the Bank of Latvia represent the Group and Bank's correspondent account balance.

All cash balances are allocated in Stage 1. Changes in ECL allowances can be specified as follows:

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
Allowances for balances due from the Bank of Latvia at the beginning of the year	9,417	9,417	8,961	8,961
Increase/(decrease) in the reporting year	1,846	1,846	(456)	(456)
Allowances for balances due from the Bank of Latvia at the end of the year	11,263	11,263	9,417	9,417

Demand deposits with the Bank of Latvia include reserves, which are held in accordance with the Regulations of the Bank of Latvia. These Regulations prescribe the minimum level of the Bank's average correspondent account balance per month, while at any given day these funds can be freely accessed and used by the Bank.

The minimum level of the Bank's correspondent account for the period from 18 December 2019 to 28 January 2020 was set at EUR 1,850,969 (2018: EUR 1,924,768). The Bank was in compliance with the reserve requirement of the Bank of Latvia in 2019 and 2018.

12. Balances due from banks

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
Due from banks registered in Latvia	71	71	688	688
Due from banks registered in non-OECD countries	22,216,967	22,216,967	22,224,467	22,224,467
Due from banks registered in OECD countries	28,774,383	28,774,383	21,957,351	21,957,351
Balances due from banks, gross	**50,991,421**	**50,991,421**	**44,182,506**	**44,182,506**
ECL allowances	(640,999)	(640,999)	(50,135)	(50,135)
Balances due from banks, net	**50,350,422**	**50,350,422**	**44,132,371**	**44,132,371**

The table below discloses the balances due from banks by their type:

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
On demand	21,100,270	21,100,270	22,485,598	22,485,598
Balances with maturity of three months or less	29,876,531	29,876,531	21,638,998	21,638,998
Other balances due from banks	14,620	14,620	57,910	57,910
Balances due from banks, gross	**50,991,421**	**50,991,421**	**44,182,506**	**44,182,506**
ECL allowances	(640,999)	(640,999)	(50,135)	(50,135)
Balances due from banks, net	**50,350,422**	**50,350,422**	**44,132,371**	**44,132,371**

12. Balances due from banks *(cont'd)*

The table below discloses an analysis of changes in gross carrying amount and corresponding ECL allowance on balances due from credit institutions during the year ended 31 December 2019:

Balances due from banks	Stage 1	Stage 2	Stage 3	Total
Gross carrying amount as at 01.01.2019	**44,182,506**	**-**	**-**	**44,182,506**
New assets originated or purchased	121,988,504	-	-	121,988,504
Assets repaid	(115,548,575)	-	-	(115,548,575)
Foreign exchange adjustments	368,986	-	-	368,986
Gross carrying amount as at 31.12.2019	**50,991,421**	**-**	**-**	**50,991,421**

Balances due from banks	Stage 1	Stage 2	Stage 3	Total
ECL as at 01.01.2019	**50,135**	**-**	**-**	**50,135**
New assets originated or purchased	3,109,816	-	-	3,109,816
Assets repaid	(2,519,493)	-	-	(2,519,493)
Foreign exchange adjustments	541	-	-	541
ECL as at 31.12.2019	**640,999**	**-**	**-**	**640,999**

The table below discloses an analysis of changes in gross carrying amount and corresponding ECL allowance on balances due from credit institutions during the year ended 31 December 2019:

Balances due from banks	Stage 1	Stage 2	Stage 3	Total
Gross carrying amount as at 01.01.2018	**89,439,452**	**-**	**-**	**89,439,452**
New assets originated or purchased	329,856,801	-	-	329,856,801
Assets repaid	(375,717,898)	-	-	(375,717,898)
Reclassification*	(1,428,736)	-	-	(1,428,736)
Foreign exchange adjustments	2,032,887	-	-	2,032,887
Gross carrying amount as at 31.12.2018	**44,182,506**	**-**	**-**	**44,182,506**

Balances due from banks	Stage 1	Stage 2	Stage 3	Total
ECL as at 01.01.2018	**71,047**	**-**	**-**	**71,047**
New assets originated or purchased	943,812	-	-	943,812
Assets repaid	(748,327)	-	-	(748,327)
Reclassification*	(214,257)	-	-	(214,257)
Foreign exchange adjustments	(2,140)	-	-	(2,140)
ECL as at 31.12.2018	**50,135**	**-**	**-**	**50,135**

* Due to the cancellation of a credit institution's activity license for ABLV Bank AS in July 2018, the Group and Bank's balances of EUR 1,428,736 due to ABLV Bank were reclassified from due to credit institutions to loans and advances to customers as loans to legal entities.

The table below discloses the Group and Bank's balances due from banks by their ratings:

	31.12.2019		31.12.2018	
Rating	**Due from banks**		**Due from banks**	
	EUR	%	EUR	%
A1 to A3	1,656,517	3.25%	817,694	1,85%
Baa1 to Baa3	37,927,029	74,38%	21,413,392	48,47%
Ba1 to Ba3	1,422	0.00%	11,323,182	25,63%
B1 to B3	579,974	1,14%	91,573	0,21%
Below B3	10,811,787	21,20%	10,478,067	23,71%
	50,976,729	**99,97%**	**44,123,908**	**99,87%**
Without rating	14,692	0.03%	58,598	0,13%
ECL allowances	(640,999)	-	(50,135)	-
Balances due from banks, net	**50,350,422**	**100%**	**44,132,371**	**100%**

Notes to the financial statements *(cont'd)*

13. Loans and advances to customers

Analysis of loans by customer profile and type of loans:

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
Loans to legal entities	62,943,049	67,513,861	101,322,199	104,084,869
Loans to private individuals, except for mortgages	3,537,150	3,537,150	6,237,636	6,237,636
Mortgages	108,763	108,763	165,656	165,656
Total loans and advances to customers, gross	**66,588,962**	**71,159,774**	**107,725,491**	**110,488,161**
Allowances for loan impairment	(11,834,245)	(11,861,972)	(22,227,012)	(22,227,707)
Total loans and advances to customers, net	**54,754,717**	**59,297,802**	**85,498,479**	**88,260,454**

The table below discloses an analysis of changes in gross carrying amount and corresponding ECL allowance on balances of the Group's loans and advances to customer during the year ended 31 December 2019.

Loans to legal entities	Stage 1	Stage 2	Stage 3	Total
Gross carrying amount as at 01.01.2019	**58,392,313**	**18,252,004**	**24,677,882**	**101,322,199**
New assets originated or purchased	103,122,471	3,498,247	62,472	106,683,190
Assets repaid	(116,475,060)	(14,561,948)	(4,578,960)	(135,615,968)
Assets sold	-	(3,271,242)	-	(3,271,242)
Transfers to Stage 2	(2,637,319)	2,637,319	-	-
Transfers to Stage 3	(101)	(401,510)	401,611	-
Amounts written off	-	-	(7,684,246)	(7,684,246)
Foreign exchange adjustments	1,070,640	333,493	104,983	1,509,116
Gross carrying amount as at 31.12.2019	**43,472,944**	**6,486,363**	**12,983,742**	**62,943,049**

Loans to legal entities	Stage 1	Stage 2	Stage 3	Total
ECL as at 01.01.2019	**824,935**	**2,318,224**	**15,874,385**	**19,017,544**
New assets originated or purchased	2,336,185	1,221,374	180,314	3,737,873
Assets repaid	(1,951,367)	(2,808,085)	(548,276)	(5,307,728)
Assets sold	-	(97,596)	-	(97,596)
Transfers to Stage 2	(11,439)	11,439	-	-
Transfers to Stage 3	-	(93,899)	93,899	-
Amounts written off	-	-	(7,684,246)	(7,684,246)
Foreign exchange adjustments	12,103	53,162	71,553	136,818
ECL as at 31.12.2019	**1,210,417**	**604,619**	**7,987,629**	**9,802,665**

Loans to private individuals, except for mortgages	Stage 1	Stage 2	Stage 3	Total
Gross carrying amount as at 01.01.2019	**45,723**	**5,442,833**	**749,080**	**6,237,636**
New assets originated or purchased	554,077	489,018	422	1,043,517
Assets repaid	(585,968)	(2,601,411)	(17,975)	(3,205,354)
Transfers to Stage 2	(18)	18	-	-
Transfers to Stage 3	(376)	-	376	-
Amounts written off	-	-	(538,806)	(538,806)
Foreign exchange adjustments	157	-	-	157
Gross carrying amount as at 31.12.2019	**13,595**	**3,330,458**	**193,097**	**3,537,150**

13. Loans and advances to customers *(cont'd)*

Loans to private individuals, except for mortgages	Stage 1	Stage 2	Stage 3	Total
ECL as at 01.01.2019	**1,158**	**2,447,866**	**749,081**	**3,198,105**
New assets originated or purchased	12,904	708,374	373	721,651
Assets repaid	(13,594)	(1,332,681)	(17,381)	(1,363,656)
Amounts written off	-	-	(538,977)	(538,977)
ECL as at 31.12.2019	**468**	**1,823,559**	**193,096**	**2,017,123**

Mortgages	Stage 1	Stage 2	Stage 3	Total
Gross carrying amount as at 01.01.2019	**154,972**	**-**	**10,684**	**165,656**
New assets originated or purchased	9,607	-	3,143	12,750
Assets repaid	(72,153)	-	(18)	(72,171)
Foreign exchange adjustments	2,528	-	-	2,528
Gross carrying amount as at 31.12.2019	**94,954**	**-**	**13,809**	**108,763**

Mortgages	Stage 1	Stage 2	Stage 3	Total
ECL as at 01.01.2019	**679**	**-**	**10,684**	**11,363**
New assets originated or purchased	491	-	3,143	3,634
Assets repaid	(536)	-	(18)	(554)
Foreign exchange adjustments	14	-	-	14
ECL as at 31.12.2019	**648**	**-**	**13,809**	**14,457**

The table below discloses an analysis of changes in gross carrying amount and corresponding ECL allowance on balances of the Bank's loans and advances to customer during the year ended 31 December 2019.

Loans to legal entities	Stage 1	Stage 2	Stage 3	Total
Gross carrying amount as at 01.01.2019	**61,154,983**	**18,252,004**	**24,677,882**	**104,084,869**
New assets originated or purchased	106,307,282	3,498,247	62,472	109,868,001
Assets repaid	(117,851,729)	(14,561,948)	(4,578,960)	(136,992,637)
Assets sold	-	(3,271,242)	-	(3,271,242)
Transfers to Stage 2	(2,637,319)	2,637,319	-	-
Transfers to Stage 3	(101)	(401,510)	401,611	-
Amounts written off	-	-	(7,684,246)	(7,684,246)
Foreign exchange adjustments	1,070,640	333,493	104,983	1,509,116
Gross carrying amount as at 31.12.2019	**48,043,756**	**6,486,363**	**12,983,742**	**67,513,861**

Loans to legal entities	Stage 1	Stage 2	Stage 3	Total
ECL as at 01.01.2019	**825,630**	**2,318,224**	**15,874,385**	**19,018,239**
New assets originated or purchased	2,434,120	1,221,374	180,314	3,835,808
Assets repaid	(2,022,270)	(2,808,085)	(548,276)	(5,378,631)
Assets sold	-	(97,596)	-	(97,596)
Transfers to Stage 2	(11,439)	11,439	-	-
Transfers to Stage 3	-	(93,899)	93,899	-
Amounts written off	-	-	(7,684,246)	(7,684,246)
Foreign exchange adjustments	12,103	53,162	71,553	136,818
ECL as at 31.12.2019	**1,238,144**	**604,619**	**7,987,629**	**9,830,392**

Loans to private individuals, except for mortgages	Stage 1	Stage 2	Stage 3	Total
Gross carrying amount as at 01.01.2019	**45,723**	**5,442,833**	**749,080**	**6,237,636**
New assets originated or purchased	554,077	489,018	422	1,043,517
Assets repaid	(585,968)	(2,601,411)	(17,975)	(3,205,354)
Transfers to Stage 2	(18)	18	-	-
Transfers to Stage 3	(376)	-	376	-
Amounts written off	-	-	(538,806)	(538,806)
Foreign exchange adjustments	157	-	-	157
Gross carrying amount as at 31.12.2019	**13,595**	**3,330,458**	**193,097**	**3,537,150**

13. Loans and advances to customers *(cont'd)*

Loans to private individuals, except for mortgages	Stage 1	Stage 2	Stage 3	Total
ECL as at 01.01.2019	**1,158**	**2,447,866**	**749,081**	**3,198,105**
New assets originated or purchased	12,904	708,374	373	721,651
Assets repaid	(13,594)	(1,332,681)	(17,381)	(1,363,656)
Amounts written off	-	-	(538,977)	(538,977)
ECL as at 31.12.2019	**468**	**1,823,559**	**193,096**	**2,017,123**

Mortgages	Stage 1	Stage 2	Stage 3	Total
Gross carrying amount as at 01.01.2019	**154,972**	**-**	**10,684**	**165,656**
New assets originated or purchased	9,607	-	3,143	12,750
Assets repaid	(72,153)	-	(18)	(72,171)
Foreign exchange adjustments	2,528	-	-	2,528
Gross carrying amount as at 31.12.2019	**94,954**	**-**	**13,809**	**108,763**

Mortgages	Stage 1	Stage 2	Stage 3	Total
ECL as at 01.01.2019	**679**	**-**	**10,684**	**11,363**
New assets originated or purchased	491	-	3,143	3,634
Assets repaid	(536)	-	(18)	(554)
Foreign exchange adjustments	14	-	-	14
ECL as at 31.12.2019	**648**	**-**	**13,809**	**14,457**

The table below discloses an analysis of changes in gross carrying amount and corresponding ECL allowance on balances of the Group's loans and advances to customer during the year ended 31 December 2018.

Loans to legal entities	Stage 1	Stage 2	Stage 3	Total
Gross carrying amount as at 01.01.2018	**58,226,142**	**20,258,440**	**33,823,607**	**112,308,189**
New assets originated or purchased	106,790,297	10,838,046	419,776	118,048,119
Assets repaid	(90,175,110)	(31,078,330)	(2,698,299)	(123,951,739)
Reclassification*	1,428,736	-	-	1,428,736
Assets sold	-	-	(9,952,684)	(9,952,684)
Transfers to Stage 1	906,377	(906,377)	-	-
Transfers to Stage 2	(20,961,305)	20,961,305	-	-
Transfers to Stage 3	(62,130)	(2,655,476)	2,717,606	-
Amounts written off	-	-	(172,219)	(172,219)
Foreign exchange adjustments	2,239,306	834,396	540,095	3,613,797
Gross carrying amount as at 31.12.2018	**58,392,313**	**18,252,004**	**24,677,882**	**101,322,199**

Loans to legal entities	Stage 1	Stage 2	Stage 3	Total
ECL as at 01.01.2018	**1,248,482**	**2,494,253**	**24,078,733**	**27,821,468**
New assets originated or purchased	1,922,318	4,985,556	1,860,747	8,768,621
Assets repaid	(2,228,461)	(5,155,523)	(3,084,213)	(10,468,197)
Reclassification*	214,257	-	-	214,257
Assets sold	-	-	(7,734,827)	(7,734,827)
Transfers to Stage 1	138,228	(138,228)	-	-
Transfers to Stage 2	(512,812)	512,812	-	-
Transfers to Stage 3	(2,195)	(457,851)	460,046	-
Amounts written off	-	-	(172,219)	(172,219)
Foreign exchange adjustments	45,118	77,205	466,118	588,441
ECL as at 31.12.2018	**824,935**	**2,318,224**	**15,874,385**	**19,017,544**

* Due to the cancellation of a credit institution's activity license for ABLV Bank AS in July 2018, the Group and Bank's balances of EUR 1,428,736 due to ABLV Bank were reclassified from due to credit institutions to loans and advances to customers as loans to legal entities.

13. Loans and advances to customers *(cont'd)*

Loans to private individuals, except for mortgages	Stage 1	Stage 2	Stage 3	Total
Gross carrying amount as at 01.01.2018	**195,943**	**7,535,734**	**3,047,105**	**10,778,782**
New assets originated or purchased	420,032	775,806	564	1,196,402
Assets repaid	(429,009)	(3,015,739)	(15,389)	(3,460,137)
Assets sold	-	-	(2,294,372)	(2,294,372)
Transfers to Stage 1	12,254	(12,254)	-	-
Transfers to Stage 2	(149,332)	149,332	-	-
Transfers to Stage 3	(1,219)	(11)	1,230	-
Amounts written off	-	-	(21,796)	(21,796)
Foreign exchange adjustments	(2,946)	9,965	31,738	38,757
Gross carrying amount as at 31.12.2018	**45,723**	**5,442,833**	**749,080**	**6,237,636**

Loans to private individuals, except for mortgages	Stage 1	Stage 2	Stage 3	Total
ECL as at 01.01.2018	**9,598**	**1,688,840**	**2,935,527**	**4,633,965**
New assets originated or purchased	10,417	1,962,218	58,359	2,030,994
Assets repaid	(13,130)	(1,210,038)	(71,961)	(1,295,129)
Assets sold	-	-	(2,185,307)	(2,185,307)
Transfers to Stage 1	2,446	(2,446)	-	-
Transfers to Stage 2	(8,265)	8,265	-	-
Transfers to Stage 3	(7)	-	7	-
Amounts written off	-	-	(21,796)	(21,796)
Foreign exchange adjustments	99	1,027	34,252	35,378
ECL as at 31.12.2018	**1,158**	**2,447,866**	**749,081**	**3,198,105**

Mortgages	Stage 1	Stage 2	Stage 3	Total
Gross carrying amount as at 01.01.2018	**208,195**	**-**	**10,684**	**218,879**
New assets originated or purchased	11,678	2,950	-	14,628
Assets repaid	(56,110)	(17,751)	-	(73,861)
Transfers to Stage 1	115,092	(115,092)	-	-
Transfers to Stage 2	(128,429)	128,429	-	-
Foreign exchange adjustments	4,546	1,464	-	6,010
Gross carrying amount as at 31.12.2018	**154,972**	**-**	**10,684**	**165,656**

Mortgages	Stage 1	Stage 2	Stage 3	Total
ECL as at 01.01.2018	**2,135**	**-**	**10,684**	**12,819**
New assets originated or purchased	641	6,608	-	7,249
Assets repaid	(7,739)	(1,122)	-	(8,861)
Transfers to Stage 1	7,313	(7,313)	-	-
Transfers to Stage 2	(1,733)	1,733	-	-
Foreign exchange adjustments	62	94	-	156
ECL as at 31.12.2018	**679**	**-**	**10,684**	**11,363**

Notes to the financial statements *(cont'd)*

13. Loans and advances to customers *(cont'd)*

The table below discloses an analysis of changes in gross carrying amount and corresponding ECL allowance on balances of the Bank's loans and advances to customer during the year ended 31 December 2018.

Loans to legal entities	Stage 1	Stage 2	Stage 3	Total
Gross carrying amount as at 01.01.2018	**60,726,975**	**20,258,440**	**33,823,607**	**114,809,022**
New assets originated or purchased	107,158,591	10,838,046	419,776	118,416,413
Assets repaid	(90,281,567)	(31,078,330)	(2,698,299)	(124,058,196)
Reclassification*	1,428,736	-	-	1,428,736
Assets sold	-	-	(9,952,684)	(9,952,684)
Transfers to Stage 1	906,377	(906,377)	-	-
Transfers to Stage 2	(20,961,305)	20,961,305	-	-
Transfers to Stage 3	(62,130)	(2,655,476)	2,717,606	-
Amounts written off	-	-	(172,220)	(172,220)
Foreign exchange adjustments	2,239,306	834,396	540,096	3,613,798
Gross carrying amount as at 31.12.2018	**61,154,983**	**18,252,004**	**24,677,882**	**104,084,869**

Loans to legal entities	Stage 1	Stage 2	Stage 3	Total
ECL as at 01.01.2018	**1,248,482**	**2,494,253**	**24,078,733**	**27,821,468**
New assets originated or purchased	1,936,042	4,985,556	1,860,747	8,782,345
Assets repaid	(2,241,490)	(5,155,523)	(3,084,213)	(10,481,226)
Reclassification*	214,257	-	-	214,257
Assets sold	-	-	(7,734,827)	(7,734,827)
Transfers to Stage 1	138,228	(138,228)	-	-
Transfers to Stage 2	(512,812)	512,812	-	-
Transfers to Stage 3	(2,195)	(457,851)	460,046	-
Amounts written off	-	-	(172,219)	(172,219)
Foreign exchange adjustments	45,118	77,205	466,118	588,441
ECL as at 31.12.2018	**825,630**	**2,318,224**	**15,874,385**	**19,018,239**

* Due to the cancellation of a credit institution's activity license for ABLV Bank AS in July 2018, the Group and Bank's balances of EUR 1,428,736 due to ABLV Bank were reclassified from due to credit institutions to loans and advances to customers as loans to legal entities.

Loans to private individuals, except for mortgages	Stage 1	Stage 2	Stage 3	Total
Gross carrying amount as at 01.01.2018	**195,943**	**7,535,734**	**3,047,105**	**10,778,782**
New assets originated or purchased	420,032	775,806	564	1,196,402
Assets repaid	(429,009)	(3,015,739)	(15,389)	(3,460,137)
Assets sold	-	-	(2,294,372)	(2,294,372)
Transfers to Stage 1	12,254	(12,254)	-	-
Transfers to Stage 2	(149,332)	149,332	-	-
Transfers to Stage 3	(1,219)	(11)	1,230	-
Amounts written off	-	-	(21,796)	(21,796)
Foreign exchange adjustments	(2,946)	9,965	31,738	38,757
Gross carrying amount as at 31.12.2018	**45,723**	**5,442,833**	**749,080**	**6,237,636**

Loans to private individuals, except for mortgages	Stage 1	Stage 2	Stage 3	Total
ECL as at 01.01.2018	**9,598**	**1,688,840**	**2,935,527**	**4,633,965**
New assets originated or purchased	10,417	1,962,218	58,359	2,030,994
Assets repaid	(13,130)	(1,210,038)	(71,961)	(1,295,129)
Assets sold	-	-	(2,185,307)	(2,185,307)
Transfers to Stage 1	2,446	(2,446)	-	-
Transfers to Stage 2	(8,265)	8,265	-	-
Transfers to Stage 3	(7)	-	7	-
Amounts written off	-	-	(21,796)	(21,796)
Foreign exchange adjustments	99	1,027	34,252	35,378
ECL as at 31.12.2018	**1,158**	**2,447,866**	**749,081**	**3,198,105**

Notes to the financial statements *(cont'd)*

13. Loans and advances to customers *(cont'd)*

Mortgages	Stage 1	Stage 2	Stage 3	Total
Gross carrying amount as at 01.01.2018	**208,195**	**-**	**10,684**	**218,879**
New assets originated or purchased	11,678	2,950	-	14,628
Assets repaid	(56,110)	(17,751)	-	(73,861)
Transfers to Stage 1	115,092	(115,092)	-	-
Transfers to Stage 2	(128,429)	128,429	-	-
Foreign exchange adjustments	4,546	1,464	-	6,010
Gross carrying amount as at 31.12.2018	**154,972**	**-**	**10,684**	**165,656**

Mortgages	Stage 1	Stage 2	Stage 3	Total
ECL as at 01.01.2018	**2,135**	**-**	**10,684**	**12,819**
New assets originated or purchased	641	6,608	-	7,249
Assets repaid	(7,739)	(1,122)	-	(8,861)
Transfers to Stage 1	7,313	(7,313)	-	-
Transfers to Stage 2	(1,733)	1,733	-	-
Foreign exchange adjustments	62	94	-	156
ECL as at 31.12.2018	**679**	**-**	**10,684**	**11,363**

Risk concentration in the loan portfolio by industry profile:

	31.12.2019 Group EUR	%	31.12.2019 Bank EUR	%	31.12.2018 Group EUR	%	31.12.2018 Bank EUR	%
Trade and commercial activities	21,433,557	32,19	21,433,557	30,12	37,535,022	34,84	37,535,022	33,97
Transport and communications	20,253,885	30,42	20,253,885	28,46	32,039,854	29,74	32,039,854	29,00
Construction and operations with real estate	8,377,738	12,58	12,948,550	18,20	16,633,959	15,44	19,396,629	17,56
Manufacturing	3,823,132	5,74	3,823,132	5,37	5,488,419	5,10	5,488,419	4,97
Private individuals	3,645,913	5,48	3,645,913	5,12	6,403,292	5,94	6,403,292	5,80
Financial services	2,981,978	4,48	2,981,978	4,19	4,004,905	3,72	4,004,905	3,62
Information and communications services	2,020,385	3,03	2,020,385	2,84	-	-	-	-
Power, heat or gas supply	1,453,953	2,18	1,453,953	2,04	-	-	-	-
Other	903,491	1,36	903,491	1,27	919,817	0,85	919,817	0,83
Agriculture and food industry	858,372	1,29	858,372	1,21	4,066,677	3,78	4,066,677	3,68
Tourism and hotel services, restaurant business	424,435	0,64	424,435	0,60	633,546	0,59	633,546	0,57
Forestry and logging	412,123	0,62	412,123	0,58	-	-	-	-
Total loans and advances to customers (before impairment allowances)	**66,588,962**	**100.00**	**71,159,774**	**100.00**	**107,725,491**	**100.00**	**110,488,161**	**100.00**

As at 31 December 2019, the total amount of loans issued to the 10 largest Group and Bank's customers was EUR 44,558,037 (2018: EUR 63,271,497), which comprised 62.62% of the total credit portfolio (2018: 57.27%).

13. Loans and advances to customers *(cont'd)*

The analysis of the Group's collateral as at 31 December 2019:

	Assets with collateral value exceeding the loan balance		Assets with insufficient collateral	
	Carrying amount of asset (before impairment allowances)	Recoverable amount of collateral	Carrying amount of asset (before impairment allowances)	Recoverable amount of collateral
	EUR	EUR	EUR	EUR
Loans to legal entities	48,504,092	107,653,598	14,241,980	6,034,510
Loans to individuals – consumer loans	3,330,440	11,218,717	206,710	-
Mortgages	94,954	428,062	13,031	-
Total	**51,929,486**	**119,300,377**	**14,461,721**	**6,034,510**

The analysis of the Bank's collateral as at 31 December 2019:

	Assets with collateral value exceeding the loan balance		Assets with insufficient collateral	
	Carrying amount of asset (before impairment allowances)	Recoverable amount of collateral	Carrying amount of asset (before impairment allowances)	Recoverable amount of collateral
	EUR	EUR	EUR	EUR
Loans to legal entities	53,074,872	114,803,598	14,241,980	6,034,510
Loans to individuals – consumer loans	3,330,440	11,218,717	206,710	-
Mortgages	94,954	428,062	13,031	-
Total	**56,500,266**	**126,450,377**	**14,461,721**	**6,034,510**

The analysis of the Group's collateral as at 31 December 2018:

	Assets with collateral value exceeding the loan balance		Assets with insufficient collateral	
	Carrying amount of asset (before impairment allowances)	Recoverable amount of collateral	Carrying amount of asset (before impairment allowances)	Recoverable amount of collateral
	EUR	EUR	EUR	EUR
Loans to legal entities	68,323,101	138,073,570	32,854,170	10,267,736
Loans to individuals – consumer loans	5,452,395	12,413,009	471,668	-
Mortgages	154,973	583,349	323,046	-
Total	**73,930,469**	**151,069,928**	**33,648,884**	**10,267,736**

13. Loans and advances to customers *(cont'd)*

The analysis of the Bank's collateral as at 31 December 2018:

	Assets with collateral value exceeding the loan balance		Assets with insufficient collateral	
	Carrying amount of asset (before impairment allowances)	Recoverable amount of collateral	Carrying amount of asset (before impairment allowances)	Recoverable amount of collateral
	EUR	EUR	EUR	EUR
Loans to legal entities	68,323,101	138,073,570	35,616,766	12,935,799
Loans to individuals – consumer loans	5,452,395	12,413,009	471,668	-
Mortgages	154,973	583,349	323,046	-
Total	**73,930,469**	**151,069,928**	**36,411,480**	**12,935,799**

14. Financial assets at fair value through profit or loss

	31.12.2019	31.12.2019	31.12.2018	31.12.2018
	Group	Bank	Group	Bank
	EUR	EUR	EUR	EUR
Latvian government bonds	1,216,687	1,216,687	1,273,368	1,273,368
OECD government bonds	24,461,073	24,461,073	21,153,385	21,153,385
OECD corporate bonds	5,149,866	5,149,866	2,290,225	2,290,225
Non-OECD corporate bonds	180,139	180,139	524,700	524,700
Unquoted shares	7,959	7,959	7,808	7,808
	31,015,724	**31,015,724**	**25,249,486**	**25,249,486**

The analysis of the Group and Bank's securities by issuers' ratings:

	31.12.2019		31.12.2018	
Rating	Securities		Securities	
	EUR	%	EUR	%
Aaa to Aa3	24,772,972	79,87%	12,903,680	51,10%
A1 to A3	5,559,015	17,92%	11,331,446	44,88%
Baa1 to Baa3	675,779	2,18%	1,006,552	3,99%
Below B3	7,959	0,03%	7,808	0,03%
	31,015,725	**100%**	**25,249,486**	**100%**
Without rating	-	-	-	-
	31,015,725	**100%**	**25,249,486**	**100%**

15. Investment in subsidiary

The table below discloses the Bank's investment in its subsidiary as at 31 December 2019.

Company	Address	Share capital	Bank's interest	Equity	Assets as at 31.12.2019	(Loss) for the reporting year
Grunewald Residence SIA	Jura Alunāna Street 2, Riga, LV-1010	6,600,000	92,42%	7,018,905	12,784,387	594,885

The table below discloses the Bank's investment in its subsidiary as at 31 December 2018.

Company	Address	Share capital	Bank's interest	Equity	Assets as at 31.12.2018	(Loss) for the reporting year
Grunewald Residence SIA	Jura Alunāna Street 2, Riga, LV-1010	6,600,000	92,42%	6,424,020	9,211,287	(74,055)

At the end of 2017, a real estate – a land plot with buildings in an exclusive district of Berlin, Germany – was acquired by the subsidiary within a framework of the debt recovery procedure against a Bank's borrower. The acquisition was carried out with a view to developing and selling the property. The real estate was encumbered with rent agreements which all have been terminated at present, and more than half of the buildings have been taken into possession by the subsidiary. Some tenants had signed sub-lease agreements, and to terminate them and fully vacate the premises as well as for providing legal assistance concerning the real estate as such, the subsidiary had hired one of the leading law firms in Berlin. The legal assistance providers believe in a positive outcome as to the possibility of terminating the sub-leases in 2020 and thus preparing the real estate for the implementation of the construction project. Accordingly, the subsidiary proceeds working with the construction project of the real estate the design of which was developed by one of the leading architectural practices in Berlin and for which a construction permit was received; the execution of next stages requires cutting of trees and demolishing of buildings.

According to the estimates of an independent valuer, the value of the real estate as at the end of the year 2018 was EUR 24.6 million (see Note 19 on the estimates used in the valuation).

Given the upward tendencies in the real estate market in Berlin, it is expected that the value of the real estate owned by the subsidiary will grow. On 18 December 2018, there were sold 500,000 of the company's shares to a third party, as a result the Bank's investment into this subsidiary as at 31 December 2019 was 92.42%.

16. Intangible assets

Changes in the Group and Bank's intangible assets in 2019 and 2018 can be specified as follows:

	Software 2019 EUR	Pre-payments 2019 EUR	Total software 2019 EUR	Software 2018 EUR	Pre-payments 2018 EUR	Total software 2018 EUR
Cost						
At the beginning of the year	2,149,643	70,134	2,219,777	2,100,907	27,323	2,128,230
Additions	39,676	59,359	99,035	48,736	42,811	91,547
Disposals	-	-	-	-		
At the end of the year	**2,189,319**	**129,493**	**2,318,812**	**2,149,643**	**70,134**	**2,219,777**
Amortization						
Accumulated amortization at the beginning of the year	1,716,891	-	1,716,891	1,555,082	-	1,555,082
Charge for the year	151,376	-	151,376	161,809	-	161,809
On disposals	-	-	-	-	-	-
Accumulated amortization at the end of the year	**1,868,267**	**-**	**1,868,267**	**1,716,891**	**-**	**1,716,891**
Net carrying amount at the beginning of the year	**432,752**	**70,134**	**502,886**	**545,825**	**27,323**	**573,148**
Net carrying amount at the end of the year	**321,052**	**129,493**	**450,545**	**432,752**	**70,134**	**502,886**

As at 31 December 2019, a number of assets that have been fully amortized were still in active use. The total original cost value of these assets as at the end of the year was EUR 1,490,306 (31 December 2018: EUR 1,375,886).

Intangible assets are amortized over their estimated useful lives, not exceeding 5 years, on a straight-line basis and disclosed under the amortization and depreciation caption of the statement of comprehensive income.

17. Property and equipment, and right-of-use assets

Changes in the Group's and Bank's property and equipment in 2019 can be specified as follows:

	Land and building EUR	Transport vehicles EUR	Computers EUR	Office equipment EUR	Other assets EUR	Pre-payment EUR	Total EUR
Cost							
As at 31.12.2018	**13,335,000**	**65,179**	**1,088,761**	**604,559**	**100,927**	**11,521**	**15,205,947**
Additions	-	-	4,990	5,790	-	19,410	30,190
Disposals	-	-	(3,178)	-	-	-	(3,178)
Revaluation	-	-	-	-	-		-
As at 31.12.2019	**13,335,000**	**65,179**	**1,090,573**	**610,349**	**100,927**	**30,931**	**15,232,959**
Depreciation							
As at 31.12.2018	**150,899**	**61,046**	**905,219**	**566,924**	**61,164**	**-**	**1,745,252**
On disposals	-	-	(3,142)	-	-	-	(3,142)
Revaluation	-	-	-	-	-	-	-
Charge for 2019	150,899	4,133	157,476	13,566	6,116	-	332,190
As at 31.12.2019	**301,798**	**65,179**	**1,059,553**	**580,490**	**67,280**	**-**	**2,074,300**
Net carrying amount as at 31.12.2018	**13,184,101**	**4,133**	**183,542**	**37,635**	**39,763**	**11,521**	**13,460,695**
Net carrying amount as at 31.12.2019	**13,033,202**	**-**	**31,020**	**29,859**	**33,647**	**30,931**	**13,158,659**

As at 31 December 2019, a number of assets that have been fully depreciated were still in active use. The total original cost value of these assets as at the end of the year was EUR 1,293,734 (31 December 2018: EUR 1,123,567).

Depreciation is calculated on a straight-line basis over the estimated useful life of the asset applying the depreciation rates established by the management and disclosed under the amortization and depreciation caption of the statement of comprehensive income.

At the end of the year 2019, the Bank revaluated the building on the basis of a valuation carried out by an independent certified valuator in accordance with international standards. The fair value of the building was determined using the comparable sales approach and income approach. Under the income approach, direct capitalization rate of 6% was used. The forecasts were based on the rental income. As a result of the revaluation, the Bank's building value was set at EUR 13,410 million.

The Group and the Bank have entered into lease agreements on premises that are used in their business activities. The leases term is 3 to 5 years. The Group and the Bank's lease liabilities are secured with the leased assets (see also Note 23). The Group has also several car lease agreements for 12 months or less and low value office equipment lease agreements. The Group applies the short-term lease and low-value asset lease exemption to the said lease agreements.

Carrying amounts of recognized right-of-use assets and changes therein:

	Premises EUR	Total EUR
Right-of-use assets as at 1 January 2019	**109,846**	**109,846**
Additions	15,239	15,239
Depreciation	(36,008)	(36,008)
Foreign exchange adjustments	2,803	2,803
Right-of-use assets as at 31 December 2019	**91,880**	**91,880**

17. Property and equipment, and right-of-use assets *(cont'd)*

Amounts recognized in the statement of comprehensive income in 2019:

	EUR
Depreciation of right-of-use assets	(36,008)
Lease interest expense	(3,620)
Expense related to short-term and low value asset leases (included in administrative expense)	(9,297)
Total amount recognized in the statement of comprehensive income	**(48,925)**

The Group and Bank's total lease payments in 2019 amounted to EUR 38,686.

Changes in the Group's and Bank's property and equipment in 2018 can be specified as follows:

	Land and building EUR	Transport vehicles EUR	Computers EUR	Office equipment EUR	Other assets EUR	Pre-payment EUR	Total EUR
Cost							
As at 31.12.2017	**13,335,313**	**89,012**	**1,195,212**	**602,596**	**100,927**	**9,548**	**15,332,608**
Additions	-	-	6,208	1,972	-	1,973	10,153
Disposals	-	(23,833)	(112,659)	(322)	-	-	(136,814)
Reclassified	(313)	-	-	313	-	-	-
Revaluation	-	-	-	-	-	-	-
As at 31.12.2018	**13,335,000**	**65,179**	**1,088,761**	**604,559**	**100,927**	**11,521**	**15,205,947**
Depreciation							
As at 31.12.2017	**-**	**73,097**	**835,055**	**547,401**	**55,048**	**-**	**1,510,601**
On disposals	-	(23,833)	(112,315)	(322)	-	-	(136,470)
Revaluation	-	-	-	-	-	-	-
Charge for 2018	150,899	11,782	182,479	19,845	6,116	-	371,121
As at 31.12.2018	**150,899**	**61,046**	**905,219**	**566,924**	**61,164**	**-**	**1,745,252**
Net carrying amount as at 31.12.2017	**13,335,313**	**15,915**	**360,157**	**55,195**	**45,879**	**9,548**	**13,822,007**
Net carrying amount as at 31.12.2018	**13,184,101**	**4,133**	**183,542**	**37,635**	**39,763**	**11,521**	**13,460,695**

As at 31 December 2018, a number of assets that have been fully amortized are still in active use. The total original cost value of these assets as at the end of the year was EUR 1,123,567 (31 December 2017: EUR 1,258,363).

Depreciation is calculated on a straight-line basis over the estimated useful life of the asset applying the depreciation rates established by the management and disclosed under the amortization and depreciation caption of the statement of comprehensive income.

At the end of the year 2018, the Bank performed the revaluation of the building on the basis of a valuation carried out by an independent certified valuator in accordance with international standards. The fair value of the building was determined using the income approach method. The expected 2-year cash flow was discounted applying a discount rate of 7%; the reversion capitalization rate was 6%. The forecasts were based on the rental income. As a result of the revaluation, the Bank's building value was set at EUR 13,410 million. EUR.

The sensitivity analysis reveals that decrease or increase of the discount rate by 1% would increase the value of the Bank's building by EUR 250,000 or decrease by EUR 240,000.

18. Equity instruments at fair value through other comprehensive income

Equity instruments at fair value through other comprehensive income represent the VISA Inc preference shares obtained by the Bank in the context of the sale of shares of VISA Europe Limited to VISA Inc.

19. Other assets

Other assets in breakdown between financial assets and non-financial assets can be specified as follows:

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
Financial assets, incl.:	9,366,209	7,021,120	5,885,247	5,869,670
– Security deposits	3,613,340	1,293,340	1,259,501	1,259,501
– Accounts receivable	51,933	29,379	256,613	246,036
– Interbank settlements in progress	556,401	556,400	102,865	102,865
– Other financial assets	5,144,535	5,142,001	4,266,268	4,261,268
Non-financial assets	14,795,673	4,810,499	12,579,140	3,390,613
– repossessed collaterals	13,312,078	3,326,904	11,354,969	2,166,442
– Investment gold	1,483,595	1,483,595	1,224,171	1,224,171
Total other assets, gross	**24,161,882**	**11,831,619**	**18,464,387**	**9,260,283**
Impairment allowances for financial assets	(18,982)	(18,982)	(91,987)	(91,987)
Total other assets, net:	**24,142,900**	**11,812,637**	**18,372,400**	**9,168,296**

The analysis of the changes in the ECLs associated with other financial assets for the year ended 31 December 2019 is as follows:

	Stage 1	Stage 2	Stage 3	Total
ECL as at 1 January 2019	**5,627**	**-**	**86,360**	**91,987**
New assets originated or purchased	-	-	218,895	218,895
Assets repaid	(3,499)	-	(287,277)	(290,776)
Transfers to Stage 1	-	-	-	-
Transfers to Stage 2	(625)	625	-	-
Transfers to Stage 3	-	-	-	-
Amounts written off	-	-	(1,350)	(1,350)
Foreign exchange adjustments	226	-	-	226
ECL as at 31 December 2019	**1,729**	**625**	**16,628**	**18,982**

The analysis of the changes in the ECLs associated with other financial assets for the year ended 31 December 2018 is as follows:

	Stage 1	Stage 2	Stage 3	Total
ECL as at 1 January 2018	**361**	**-**	**17,285**	**17,646**
New assets originated or purchased	5,491	-	78,247	83,738
Transfers to Stage 3	(187)	-	187	-
Amounts written off	(38)	-	(9,359)	(9,397)
ECL as at 31 December 2018	**5,627**	**-**	**86,360**	**91,987**

19. Other assets *(cont'd)*

In non-financial assets the Group and Bank include assets obtained through repossessing collaterals which had served as security for loans and are intended for sale. The repossessed assets include private property and land plots in Latvia and Ukraine and for the Group – also in Germany (see Note 15). Non-financial assets are is stated at inventories at lower of cost and net realizable value determined according to the valuation carried out by an independent certified valuer in accordance with international standards.

The table below summarizes the methods used by the Group and Bank in determining the fair value of non-financial assets.

No	Property	Municipality	City/ pagasts	Carrying amount EUR	Methods used in fair value measurement
1	Land	Riga	Riga	22,000	Market (comparables) approach
2	Apartment	Riga	Riga	174,300	Market (comparables) approach
3	Warehouse and production premises	Kiev	Fastov	289,787	Market (comparables) approach
4	Multi-apartment building	Riga	Riga	507,094	Income approach
5	Office premises	Odes	Odes	1,005,478	Market (comparables) approach
6	Office premises	Riga	Riga	1,328,245	Market (comparables) approach and income approach
Total assets repossessed by the Bank				3,326,904	
7	Land	Berlin	Berlin	9,985,174	Income approach
Total assets repossessed by the Group				13,312,078	

20. Cash and cash equivalents

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
Cash and balances with the Bank of Latvia (Note 11)	113,359,519	113,359,519	95,098,162	95,098,162
Balances due form other banks with original maturity of 3 months or less	50,945,451	50,945,451	44,080,337	44,080,337
Total	**164,304,970**	**164,304,970**	**139,178,499**	**139,178,499**

21. Deposits from customers

(a) Analysis of deposits by customer profile

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
Legal entities				
– - current/ settlement accounts	148,318,628	148,772,751	162,160,399	162,167,582
– - term deposits	5,665,073	5,665,073	10,042,703	10,042,703
Private individuals				
– - current/ settlement accounts	29,730,419	29,730,419	42,653,555	42,653,555
– - term deposits	38,244,933	38,244,933	2,973,786	2,973,786
Total deposits from customers:	**221,959,053**	**222,413,176**	**217,830,443**	**217,837,626**
Sector:				
Private companies	120,746,648	121,200,771	138,756,333	138,763,516
Private individuals	67,975,353	67,975,353	45,627,341	45,627,341
Financial institutions	33,023,194	33,023,194	33,213,991	33,213,991
Non-profit institutions	205,342	205,342	199,664	199,664
Institutions of financial institutions and money lenders	8,516	8,516	33,114	33,114
Total deposits from customers:	**221,959,053**	**222,413,176**	**217,830,443**	**217,837,626**

(b) Analysis of deposits by place of residence

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
Residents	45,987,268	46,441,391	50,907,699	50,914,881
Non-residents	175,971,785	175,971,785	166,922,744	166,922,744
Total deposits from customers:	**221,959,053**	**222,413,176**	**217,830,443**	**217,837,625**

The average interest rate on term deposits in 2019 was 3.48% (2018: 3.72%) and the average interest rate on demand deposits was 0.00% (2018: 0.00%). All deposits bear a fixed interest rate.

Deposits from customers by industry can be specified as follows:

	31.12.2019 Group EUR	%	31.12.2019 Bank EUR	%	31.12.2018 Group EUR	%	31.12.2018 Bank EUR	%
Manufacturing	245,271	0,11	245,271	0,11	334,657	0,15	334,657	0,15
Construction and real estate	4,641,910	2,09	5,096,033	2,29	7,762,032	3,57	7,769,215	3,57
Trade and commercial activities	80,289,470	36,10	80,289,470	36,10	88,082,947	40,44	88,082,947	40,44
Financial and insurance services	58,622,369	26,36	58,622,369	26,36	58,017,419	26,63	58,017,419	26,63
Transport and communications	9,485,943	4,27	9,485,943	4,27	16,085,851	7,38	16,085,851	7,38
Agriculture and food industries	37,285	0,02	37,285	0,02	39,656	0,02	39,656	0,02
Private individuals	67,975,353	30,56	67,975,353	30,56	45,627,341	20,95	45,627,341	20,95
Other	661,452	0,30	661,452	0,30	1,880,540	0,86	1,880,540	0,86
Total deposits from customers	**221,959,053**		**222,413,176**		**217,830,443**	**100%**	**217,837,626**	**100%**

The total amount of deposits attributable to 20 largest depositors as at 31 December 2019 was EUR 140,831,778 (2018: EUR 118,383,493), comprising 63,32% of the Bank's total portfolio (2018: 54.34%).

22. Debt securities

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
Debt securities	17,896,420	17,896,420	17,558,810	17,558,810
	17,896,420	**17,896,420**	**17,558,810**	**17,558,810**

During 2016, the Bank issued debt securities in several tranches. The debt securities are offered through over-the-counter (OTC) trading and are not quoted on an open market.

The debt securities issued represent the following issues:

Subordinated bond series RIB SUBUSD-01/2016 issue totalling USD 2,200,000. The redemption date - 26 April 2021, the coupon rate - 4.50%, a coupon payment twice a year on 26 October and 26 April. Balance at 31 December 2019 amounted to EUR 1,974,253 (31 December 2018: EUR 1,937,009);

Subordinated bond series RIB SUBUSD-03/2016 issue totalling USD 14,300,000. The redemption date – 22 June 2021, the coupon rate – 4.50%, a coupon payment twice a year on 22 December and 22 June. Balance at 31 December 2019 amounted to EUR 12,743,535 (31 December 2018: EUR 12,503,133 EUR);

Subordinated bond series RIB SUBUSD-04/2016 issue totalling USD 3,500,000. The redemption date – 19 July 2021, the coupon rate – 4.50%, a coupon payment 2 times a year on 19 January and 19 July. Balance at 31 December 2019 amounted to EUR 3,178,632 (31 December 2018: EUR 3,118,668).

23. Other financial liabilities

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
Liability suspense account*	90,506	90,506	6,247	6,247
Settlements on behalf of a closed bank	16,585	16,585	16,585	16,585
Cash in transit	19,865	19,865	860	860
Accounts payable	1,264,854	70,185	140,215	115,618
ECL for off-balance sheet liabilities	660,976	660,976	112,053	112,054
Dividends paid	-	-	2,656,244	2,656,244
	2,052,786	**858,117**	**2,932,204**	**2,907,608**

* The liability suspense account as at 31 December 2019 and 31 December 2018 includes the amounts erroneously transferred to the Bank, which were returned to the senders at the beginning of 2020 and 2019 respectively.

24. Deferred income and accrued expense

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
Vacation pay reserve	380,211	380,211	336,010	336,010
Accrual for the guarantee fund and FCMC financing	86,865	86,865	60,544	60,544
State statutory social insurance contributions	252,495	252,495	247,895	247,895
Other accrued expense	153,018	153,018	288,835	288,835
Lease liabilities	92,982	92,982	-	-
	965,571	**965,571**	**933,284**	**933,284**

24. Deferred income and accrued expense*(cont'd)*

Carrying amount of lease expense and changes therein:

	Premises EUR	Total EUR
Lease liabilities as at 1 January 2019	**109,846**	**109,846**
Increase	15,239	15,239
Payments	(35,038)	(35,038)
Foreign exchange adjustments	2,935	2,935
Lease liabilities as at 31 December 2019	**92,982**	**92,982**

25. Derivative financial instruments

The Group and the Bank use the following derivative financial instruments: currency forwards – agreements on currency acquisition in the future, currency swaps – commitments to exchange one set of cash flow for another. The Group and Bank's credit risk represents the potential cost to replace the forward contracts if the counterparties fail to perform their obligations. To control the level of credit risk taken, the Group and the Bank assess counterparty risk using the same techniques as for its lending activities.

The notional amounts of financial instruments provide a basis for comparison with instruments recognized on the statement of financial position but do not necessarily indicate the amounts of future cash flows involved or the current fair value of the instruments, therefore, they cannot be used for determining the level of the Group and Bank's exposure to credit risk or market risk. The derivative instruments become favourable or unfavourable as a result of fluctuations in market interest rates or foreign exchange rates.

The Group and Bank's notional amounts and fair values of derivative instruments held for trading are set out in table below.

	31.12.2019			31.12.2018		
	Notional	Fair value		Notional		Fair value
	amount	Assets	Liabilities	amount	Assets	Liabilities
	EUR	EUR	EUR	EUR	EUR	EUR
Options	142,800	42,340	-	-	-	-
Total	**142,800**	**42,340**	**-**	**-**	**-**	**-**

The Group and Bank's notional amounts of derivative instruments by counterparty credit rating are set out in the table below:

	31.12.2019			31.12.2018		
	Notional		Fair value	Notional		Fair value
	amount	Assets	Liabilities	amount	Assets	Liabilities
	EUR	EUR	EUR	EUR	EUR	EUR
Without rating	142,800	42,340	-	-	-	-
Total	**142,800**	**42,340**	**-**	**-**	**-**	**-**

Notes to the financial statements *(cont'd)*

26. Share capital

The Bank's issued and fully paid share capital as at 31 December 2019 was EUR 32,334,756 (31 December 2018: EUR 32,334,762). The nominal value of one share was EUR 1.00 (31 December 2018: EUR 1.00). All shares are ordinary registered shares with voting rights. One share is one vote.

On 27 April 2016, the denomination of the share capital from the lats to the euro was registered. As a result of the denomination, a difference of EUR 6 was included in equity under reserves.

The shareholders of the Bank as at 31 December 2019 and 31 December 2018:

	31.12.2019 EUR	%	31.12.2018 EUR	%
SIA SKY Investment Holding	14,228,717	44.00	12,094,410	37,40
Yuriy Rodin	6,466,198	20.00	6,466,198	20,00
AB Pivdenny	4,449,558	13.76	4,449,558	13,76
Mark Bekker	3,418,808	10,57	3,418,808	10,57
Other shareholders (with less than 10% of shares)	3,771,475	11,67	5,905,782	18,27
Total share capital paid	**32,334,756**	**100%**	**32,334,756**	**100%**

27. Off-balance items and encumbered assets

Contingent liabilities

Contingent liabilities can be specified as follows:

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
Guarantees, incl.:	5,242,483	5,242,483	6,934,513	6,934,513
– Financial guarantees	4,806,837	4,806,837	6,639, 520	6,639, 520
– Non-financial guarantees	435,646	435,646	294,993	294,993
	5,242,483	**5,242,483**	**6,934,513**	**6,934,513**

Guarantees are secured by cash or loans which are blocked or reserved at the Group and the Bank and secure the Group and Bank's balances due from customers if the guarantee conditions are met.

Non-financial guarantees	Stage 1	Stage 2	Stage 3	Total
ECL as at 01.01.2019	**748**	**-**	**-**	**748**
Increase	268	-	-	268
Decrease	(15)	-	-	(15)
Foreign exchange adjustments	-	-	-	-
ECL as at 31.12.2019	**1,001**	**-**	**-**	**1,001**

Non-financial guarantees	Stage 1	Stage 2	Stage 3	Total
ECL as at 01.01.2018	**28,830**	**-**	**-**	**28,830**
Increase	1,194	-	-	1,194
Decrease	(29,276)	-	-	(29,276)
ECL as at 31.12.2018	**748**	**-**	**-**	**748**

Notes to the financial statements *(cont'd)*

27. Off-balance items and encumbered assets *(cont'd)*

Loan commitments

The outstanding loan commitments can be specified as follows:

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
Loan commitments	7,690,897	7,690,897	2,164,429	2,168,986
Undrawn credit lines	24,315,498	24,315,498	9,383,274	9,383,274
Total loan commitments	**32,006,395**	**32,006,395**	**11,547,703**	**11,552,260**

The total outstanding contractual amount of undrawn credit lines and guarantees does not necessarily represent future cash requirements, as these financial instruments may expire or terminate without being actually funded.

The loan commitments are denominated in the following currencies:

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
EUR	6,160,000	6,160,000	2,020,249	2,024,806
USD	1,530,897	1,530,897	144,180	144,180
Total loan commitments	**7,690,897**	**7,690,897**	**2,164,429**	**2,168,986**

The undrawn credit lines are denominated in the following currencies:

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
EUR	15,285,067	15,285,067	5,742,302	5,742,302
USD	9,030,431	9,030,431	3,640,972	3,640,972
Total undrawn credit lines	**24,315,498**	**24,315,498**	**9,383,274**	**9,383,274**

The analysis of the changes in ECL allowance in the year ended 31 December 2019 can be specified as follows:

Loan commitments	Stage 1	Stage 2	Stage 3	Total
ECL as at 01.01.2019	**65,068**	**46,239**	**-**	**111,307**
Increase	1,337,518	560,323	-	1,897,841
Decrease	(1,004,287)	(347,847)	-	(1,352,134)
Transfers to Stage 3	(941)	-	941	-
Foreign exchange adjustments	2,299	662	-	2,961
ECL as at 31.12.2019	**399,657**	**259,377**	**941**	**659,975**

The analysis of the changes in ECL allowance in the year ended 31 December 2018 can be specified as follows:

Loan commitments	Stage 1	Stage 2	Stage 3	Total
ECL as at 01.01.2018	**259,874**	**20,425**	-	**280,299**
Increase	692,117	835,643	-	1,527,760
Decrease	(1,352,977)	(352,815)	-	(1,705,792)
Transfers to Stage 1	(27,723)	27,723	-	-
Transfers to Stage 2	486,265	(486,265)	-	-
Foreign exchange adjustments	7,512	1,528	-	9,040
ECL as at 31.12.2018	**65,068**	**46,239**	**-**	**111,307**

27. Off-balance items and encumbered assets *(cont'd)*

Encumbered assets

The pledged and restricted assets can be specified as follows:

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
Balances due from banks	4,821,456	4,821,456	6,784,766	6,784,766
Other assets	6,320,924	6,320,924	4,436,378	4,436,378
Total	**11,142,380**	**11,142,380**	**11,221,144**	**11,221,144**

All encumbered assets serve as security for the Group and Bank's financial liabilities as at 31 December 2019 and 31 December 2018. The carrying amount of encumbered assets approximate their fair value both as at 31 December 2019 and as at 31 December 2018.

The encumbered assets of the Group and the Bank as at 31 December 2019 consisted of:

- Security deposits of EUR 6,320,924 for potential claims from Visa Inc, MasterCard Europe SPRL and Interactive Brokers LLC. The agreements with these organization provide for ensuring a sufficient amount of resources available in the deposit accounts with Lloyds TSB Bank plc (MasterCard Europe Sprl), U.S Bank (Visa Inc) respectively, which could cover all expenses related to the participation of the Bank in these organizations. The total amount of these encumbered assets is included under other assets.
- Security deposits of EUR 4,806,836 for the guarantees issued by the Group and the Bank. Total amount of these encumbered assets is included under the balances due from other banks.
- Security deposits of EUR 14,620 for letters of credit issued. The total amount of these encumbered assets is included under the balances due from other banks.

The encumbered assets of the Group and the Bank as at 31 December 2018 consisted of:

- Security deposits of EUR 4,436,378 for potential claims from Visa Inc, MasterCard Europe SPRL and Interactive Brokers LLC. The agreements with these organization provide for ensuring a sufficient amount of resources available in the deposit accounts with Lloyds TSB Bank plc (MasterCard Europe Sprl), U.S Bank (Visa Inc) respectively, which could cover all expenses related to the participation of the Bank in these organizations. The total amount of these encumbered assets is included under other assets.
- Security deposits of EUR 6,726,856 for the guarantees issued by the Group and the Bank. Total amount of these encumbered assets is included under the balances due from other banks.
- Security deposits of EUR 57,910 for letters of credit issued. The total amount of these encumbered assets is included under the balances due from other banks.

28. Capital adequacy

The Group's capital adequacy ratio according to the requirements of the Financial and Capital Market Commission is calculated as follows:

Description	31.12.2019 EUR	31.12.2018 EUR
Total own funds	**48,133,227**	**50,293,100**
– Tier 1 capital	40,849,926	37,639,741
– Common equity Tier 1 capital	40,849,926	37,639,741
– Tier 2 capital	7,283,301	12,653,359
Total risk exposure amount	**174,507,178**	**186,580,861**
– Risk weighted exposure amounts for credit, counterparty credit and dilution risks and free deliveries	142,501,990	153,807,198
– Total risk exposure amount for position, foreign exchange and commodities risks	3,273,600	4,158,663
– Total risk exposure amount for operational risk	28,731,588	28,615,000
– Total exposure amounts for credit valuation adjustment	-	-
Capital adequacy ratios		
– Common equity Tier 1 Capital ratio	23,41%	20,17%
– Surplus (+) / Deficit (-) of Common equity Tier 1 capital (4.5%)	32,997,103	29,243,602
– Tier 1 Capital ratio	23,41%	20,17%
– Surplus (+) / Deficit (-) of Tier 1 capital (6%)	30,379,495	26,444,889
– Total capital ratio	27,58%	26,96%
– Surplus (+) / Deficit (-) of total capital (8%)	34,172,653	35,366,631
– Capital retention reserve (%)	2.5%	2,5%
– Capital retention reserve	4,362,679	4,664,522

The Bank's capital adequacy ratio according to the requirements of the Financial and Capital Market Commission is calculated as follows:

Description	31.12.2019 EUR	31.12.2018 EUR
Total own funds	**47,180,495**	**49,962,284**
– Tier 1 capital	39,897,194	37,308,925
– Common equity Tier 1 capital	39,897,194	37,308,925
– Tier 2 capital	7,283,301	12,653,359
Total risk exposure amount	**175,066,897**	**183,617,538**
– Risk weighted exposure amounts for credit, counterparty credit and dilution risks and free deliveries	143,091,634	150,844,962
– Total risk exposure amount for position, foreign exchange and commodities risks	3,273,600	4,158,663
– Total risk exposure amount for operational risk	28,701,663	28,613,913
– Total exposure amounts for credit valuation adjustment	-	-
Capital adequacy ratios		
– Common equity Tier 1 Capital ratio	22,79%	20,32%
– Surplus (+) / Deficit (-) of Common equity Tier 1 capital (4.5%)	32,019,184	29,046,136
– Tier 1 Capital ratio	22,79%	20,32%
– Surplus (+) / Deficit (-) of Tier 1 capital (6%)	29,393,180	26,291,873
– Total capital ratio	26,95%	27,21%
– Surplus (+) / Deficit (-) of total capital (8%)	33,175,143	35,272,881
– Capital retention reserve (%)	2.5%	2.5%
– Capital retention reserve	4,376,672	4,590,438

The Group and the Bank's equity ratio and capital adequacy ratio are calculated applying the transitional arrangements to lessen the impact of IFRS 9 on capital ratios according to Regulation 2017/2395 of the European Parliament and of the Council 2017/2395. Had the transitional arrangements not been applied, the Group and the Bank's capital adequacy ratio as at 31 December 2019 would have been 25.46% and 24.82% respectively (31 December 2018: 24.73% and 24.96%).

29. Analysis of assets and liabilities by currency profile

The table below provides the analysis of the Group's assets, liabilities and shareholders' equity as at 31 December 2019 by currency profile:

	USD EUR	EUR EUR	Other EUR	Total EUR
Assets				
Cash and deposits with the Bank of Latvia	429,751	112,918,505	-	113,348,256
Balances due from banks	47,863,656	2,323,019	163,747	50,350,422
Loans and advances to customers	26,619,983	28,121,596	13,138	54,754,717
Financial assets at fair value through profit or loss	27,668,510	3,347,214	-	31,015,724
Equity instruments at fair value through other comprehensive income	-	412,205	-	412,205
Derivative financial instruments	42,340	-	-	42,340
Intangible assets	-	450,545	-	450,545
Property and equipment	-	13,250,539	-	13,250,539
Prepaid expenses	4,214	224,464	1,123	229,801
Other assets	4,789,049	17,152,062	2,201,789	24,142,900
Total assets	**107,417,503**	**178,200,149**	**2,379,797**	**287,997,449**
Liabilities and equity				
Deposits from customers	81,144,196	139,809,812	1,005,045	221,959,053
Debt securities	17,896,420	-	-	17,896,420
Deferred income and accrued expense	-	918,123	47,448	965,571
Other liabilities	247,821	1,806,097	-	2,053,918
Subordinated loans	8,748,647	-	-	8,748,647
Equity	-	36,373,840	-	36,373,840
Total liabilities and equity	**108,037,084**	**178,907,872**	**1,052,493**	**287,997,449**
Net long / (short) position for statement of financial position items	*(619,581)*	*(707,723)*	*1,327,304*	-
Off-balance sheet claims arising from foreign exchange contracts	-	-	-	-
Off-balance sheet liabilities arising from foreign exchange contracts	-	-	-	-
Net long / (short) position on foreign exchange	-	-	-	-
Net long / (short) position	**(619,581)**	**(707,723)**	**1,327,304**	**-**
As at 31 December 2018				
Total assets	**125,540,560**	**153,636,026**	**3,912,257**	**283,088,843**
Total liabilities and equity	**125,540,454**	**154,917,401**	**2,630,988**	**283,088,843**
Net long / (short) position for statement of financial position items	*106*	*(1,281,375)*	*1,281,269*	-
Off-balance sheet items arising from foreign exchange				
Off-balance sheet claims arising from foreign exchange contracts	-	-	-	-
Off-balance sheet liabilities arising from foreign exchange contracts	-	-	-	-
Net long / (short) position on foreign exchange	-	-	-	-
Net long / (short) position	**106**	**(1,281,375)**	**1,281,269**	**-**

29. Analysis of assets and liabilities by currency profile *(cont'd)*

The table below provides the analysis of the Bank's assets, liabilities and shareholders' equity as at 31 December 2019 by currency profile:

	USD EUR	EUR EUR	Other EUR	Total EUR
Assets				
Cash and deposits with the Bank of Latvia	429,751	112,918,505	-	113,348,256
Balances due from banks	47,863,656	2,323,019	163,747	50,350,422
Loans and advances to customers	26,619,983	32,664,681	13,138	59,297,802
Financial assets at fair value through profit or loss	27,668,510	3,347,214	-	31,015,724
Equity instruments at fair value through other comprehensive income	-	412,205	-	412,205
Derivative financial instruments	42,340	-	-	42,340
Intangible assets	-	450,545	-	450,545
Property and equipment	-	13,250,539	-	13,250,539
Investment in subsidiary	-	6,100,000	-	6,100,000
Prepaid expenses	4,214	224,464	1,123	229,801
Other assets	4,789,049	4,821,799	2,201,789	11,812,637
Total assets	**107,417,503**	**176,512,971**	**2,379,797**	**286,310,271**
Liabilities and equity				
Deposits from customers	81,144,196	140,263,935	1,005,045	222,413,176
Debt securities	17,896,420	-	-	17,896,420
Deferred income and accrued expense	-	918,123	47,448	965,571
Other liabilities	247,821	611,428	-	859,249
Subordinated loans	8,748,647	-	-	8,748,647
Equity	-	35,427,208	-	35,427,208
Total liabilities and equity	**108,037,084**	**177,220,694**	**1,052,493**	**286,310,271**
Net long / (short) position for statement of financial position items	*(619,581)*	*(707,723)*	*1,327,304*	-
Off-balance sheet claims arising from foreign exchange contracts	-	-	-	-
Off-balance sheet liabilities arising from foreign exchange contracts	-	-	-	-
Net long / (short) position on foreign exchange	-	-	-	-
Net long / (short) position	**(619,581)**	**(707,723)**	**1,327,304**	**-**
As at 31 December 2018				
Total assets	**125,540,560**	**153,293,897**	**3,912,257**	**282,746,714**
Total liabilities and equity	**125,540,454**	**154,575,272**	**2,630,988**	**282,746,714**
Net long / (short) position for statement of financial position items	*106*	*(1,281,375)*	*1,281,269*	-
Off-balance sheet items arising from foreign exchange				
Off-balance sheet claims arising from foreign exchange contracts	-	-	-	-
Off-balance sheet liabilities arising from foreign exchange contracts	-	-	-	-
Net long / (short) position on foreign exchange	-	-	-	-
Net long / (short) position	**106**	**(1,281,375)**	**1,281,269**	**-**

30. Analysis of assets and liabilities by maturity profile

The table below provides the analysis of the Group's assets and liabilities by contractual maturity as at 31 December 2019.

	Past due	Within 1 month	1 – 3 months	3 – 6 months	6 –12 months	1–5 years	Over 5 years and undated	Total
	EUR	EUR	EUR	EUR	EUR	EUR	EUR	EUR
Assets								
Cash and balances with the Bank of Latvia	-	113,348,256	-	-	-	-	-	113,348,256
Balances due from banks	-	44,966,843	576,743	4,806,836	-	-	-	50,350,422
Loans and advances to customers	2,506,331	1,713,470	1,349,941	2,343,353	17,974,304	28,841,075	26,243	54,754,717
Financial assets at fair value through profit or loss	-	24,461,073	180,140	178,630	360,305	5,827,617	7,959	31,015,724
Equity instruments at fair value through other comprehensive income	-	-	-	-	-	-	412,205	412,205
Intangible assets	-	-	-	-	-	-	450,545	450,545
Property and equipment	-	-	-	-	-	-	13,250,539	13,250,539
Derivative financial instruments	-	42,340	-	-	-	-	-	42,340
Prepaid Expense	-	-	-	-	229,801	-	-	229,801
Other assets	-	7,997,896	150	-	3,386,536	319	12,757,999	24,142,900
Total assets	**2,506,331**	**192,529,878**	**2,106,974**	**7,328,819**	**21,950,946**	**34,669,011**	**26,905,490**	**287,997,449**
Liabilities and equity								
Deposits from customers	-	184,351,674	15,281,713	18,612,032	2,168,076	1,545,558	-	221,959,053
Debt securities	-	63,090	-	30,232	-	17,803,098	-	17,896,420
Deferred income and accrued expense	-	-	872,589	-	2,761	-	90,221	965,571
Corporate income tax	-	1,132	-	-	-	-	-	1,132
Other liabilities	-	2,025,460		8,606	387	16,933	1,400	2,052,786
Subordinated loans	-	1,985	-	-	2,960,654	5,786,008	-	8,748,647
Equity	-	-	-	-	-	-	36,373,840	36,373,840
Liabilities and equity	-	**186,443,341**	**16,154,302**	**18,650,870**	**5,131,878**	**25,151,597**	**36,465,461**	**287,997,449**
Off-balance sheet liabilities	2,670,465	5,253	587,010	8,368,517	8,896,912	16,720,721	-	37,248,878
Liquidity	**(164,134)**	**6,081,284**	**(14,634,338)**	**(19,690,568)**	**7,922,156**	**(7,203,307)**	**(9,559,971)**	**(37,248,878)**
As at 31 December 2018								
Total assets	**4,816,304**	**153,431,707**	**10,002,663**	**10,154,564**	**48,483,510**	**10,692,396**	**45,507,699**	**283,088,843**
Total liabilities and equity	-	**208,528,924**	**2,040,240**	**5,845,924**	**3,181,246**	**30,780,062**	**32,712,447**	**283,088,843**
Off-balance sheet liabilities	-	19,735	1,834,552	8,948,516	2,893,144	4,717,152	69,117	18,482,216
Liquidity	**4,816,304**	**(55,116,952)**	**6,127,871**	**(4,639,876)**	**42,409,120**	**(24,804,818)**	**12,726,135**	**(18,482,216)**

30. Analysis of assets and liabilities by maturity profile *(cont'd)*

The table below provides the analysis of the Bank's assets and liabilities by contractual maturity as at 31 December 2019.

	Past due EUR	Within 1 month EUR	1 – 3 months EUR	3 – 6 months EUR	6 –12 months EUR	1–5 years EUR	Over 5 years and undated EUR	Total EUR
Assets								
Cash and balances with the Bank of Latvia	-	113,348,256	-	-	-	-	-	113,348,256
Balances due from banks	-	44,966,843	576,743	4,806,836	-	-	-	50,350,422
Loans and advances to customers	2,506,331	1,713,470	1,349,941	2,343,353	17,974,304	33,384,160	26,243	59,297,802
Financial assets at fair value through profit or loss	-	24,461,073	180,140	178,630	360,305	5,827,617	7,959	31,015,724
Investment in subsidiary	-	-	-	-	-	-	6,100,000	6,100,000
Equity instruments at fair value through other comprehensive income	-	-	-	-	-	-	412,205	412,205
Intangible assets	-	-	-	-	-	-	450,545	450,545
Property and equipment	-	-	-	-	-	-	13,250,539	13,250,539
Derivative financial instruments	-	42,340	-	-	-	-	-	42,340
Prepaid Expense	-	-	-	-	229,801	-	-	229,801
Other assets	-	5,652,807	150		3,386,536	319	2,772,825	11,812,637
Total assets	**2,506,331**	**190,184,789**	**2,106,974**	**7,328,819**	**21,950,946**	**39,212,096**	**23,020,316**	**286,310,271**
Liabilities and equity								
Deposits from customers	-	184,805,797	15,281,713	18,612,032	2,168,076	1,545,558	-	222,413,176
Debt securities	-	63,090	-	30,232	-	17,803,098	-	17,896,420
Deferred income and accrued expense	-	-	872,589	-	2,761	-	90,221	965,571
Corporate income tax	-	1,132	-	-	-	-	-	1,132
Other liabilities	-	830,791	-	8,606	387	16,933	1,400	858,117
Subordinated loans	-	1,985	-	-	2,960,654	5,786,008	-	8,748,647
Equity	-	-	-	-	-	-	35,427,208	35,427,208
Liabilities and equity	-	**185,702,795**	**16,154,302**	**18,650,870**	**5,131,878**	**25,151,597**	**35,518,829**	**286,310,271**
Off-balance sheet Liabilities	2,670,465	5,253	587,010	8,368,517	8,896,912	16,720,721	-	37,248,878
Liquidity	**(164,134)**	**4,476,741**	**(14,634,338)**	**(19,690,568)**	**7,922,156**	**(2,660,222)**	**(12,498,513)**	**(37,248,878)**
As at 31 December 2018								
Total assets	**4,816,304**	**153,416,130**	**10,002,663**	**10,154,564**	**48,483,510**	**13,454,371**	**42,419,172**	**282,746,714**
Total liabilities and equity	**-**	**208,511,511**	**2,040,240**	**5,845,924**	**3,181,246**	**30,780,062**	**32,387,731**	**282,746,714**
Off-balance sheet liabilities		19,735	1,834,552	8,948,516	2,893,144	4,721,709	69,117	18,486,773
Liquidity	**4,816,304**	**(55,115,116)**	**6,127,871**	**(4,639,876)**	**42,409,120**	**(22,047,400)**	**9,962,324**	**(18,486,773)**

30. Analysis of assets and liabilities by maturity profile *(cont'd)*

The management of the Group and the Bank believes that short-term liquidity is not endangered. The Bank's liquidity ratio calculated according to the FCMC requirements was 87.03% as at 31 December 2018 (31 December 2017: 69.29%). In accordance with the FCMC requirements, the Bank has to ensure a sufficient amount of liquid assets to settle its liabilities, but not less than 40% of the total amount of its current liabilities.

Deposits serving as security for customer liabilities are disclosed according to the maturity of the underlying liability.

The table below presents the Group's contractual undiscounted cash flows of the financial liabilities as at 31 December 2019:

	Past due	Within 1 month	1 – 3 months	3 – 6 months	6 –12 months	1–5 years	Over 5 years and undated	Total
	EUR	EUR	EUR	EUR	EUR	EUR	EUR	EUR
Debt securities	-	126,179	-	60,464	-	17,803,098	-	17,989,741
Deposits from customers	-	184,418,028	15,357,973	18,710,285	2,193,798	1,572,604	-	222,252,688
Other liabilities	-	2,025,460	-	8,606	387	16,933	1,400	2,052,786
Subordinated loans	-	41,132	75,768	114,916	3,114,719	5,871,760	-	9,218,295
Total liabilities	-	**186,610,799**	**15,433,741**	**18,894,271**	**5,308,904**	**25,264,395**	**1,400**	**251,513,510**
Off-balance sheet liabilities	-	5,253	587,010	8,368,517	8,896,912	16,720,721	2,670,465	37,248,878

The table below presents the Bank's contractual undiscounted cash flows of the financial liabilities as at 31 December 2019:

	Past due	Within 1 month	1 – 3 months	3 – 6 months	6 –12 months	1–5 years	Over 5 years and undated	Total
	EUR	EUR	EUR	EUR	EUR	EUR	EUR	EUR
Debt securities	-	126,179	-	60,464	-	17,803,098	-	17,989,741
Deposits from customers	-	184,872,151	15,357,973	18,710,285	2,193,798	1,572,604	-	222,706,811
Other liabilities	-	830,791	-	8,606	387	16,933	1,400	858,117
Subordinated loans	-	41,132	75,768	114,916	3,114,719	5,871,760	-	9,218,295
Total liabilities	-	**185,870,253**	**15,433,741**	**18,894,271**	**5,308,904**	**25,264,395**	**1,400**	**250,772,964**
Off-balance sheet liabilities	-	5,253	587,010	8,368,517	8,896,912	16,720,721	2,670,465	37,248,878

The table below presents the Group and Bank's undiscounted future lease payments as at 31 December 2019:

	31.12.2019. Group	31.12.2019. Bank	31.12.2018. Group	31.12.2018. Bank
	EUR	EUR	EUR	EUR
Maturing in less than one year	31,824	31,824	34,492	34,492
Maturing between one and five years	65,478	65,478	81,142	81,142
Maturing in more than five years	-	-	-	-
Total lease liabilities	**97,302**	**97,302**	**115,634**	**115,634**

30. Analysis of assets and liabilities by maturity profile *(cont'd)*

The table below presents the Group and Bank's contractual undiscounted cash flows of the derivative financial instruments as at 31 December 2019:

	Within 1 month	1 - 3 months	Over 3 months	Total
	EUR	EUR	EUR	EUR
Derivatives offset on a gross basis				
Foreign exchange derivatives:				
Inflow	142,800	-	-	**142,800**
Outflow	142,800	-	-	**142,800**

The table below presents the Group's contractual undiscounted cash flows of the financial liabilities as at 31 December 2018:

	Past due	Within 1 month	1 – 3 months	3 – 6 months	6 –12 months	1–5 years	Over 5 years and undated	Total
	EUR	EUR	EUR	EUR	EUR	EUR	EUR	EUR
Debt securities	-	123,799	-	59,324	-	17,467,249	-	17,650,372
Deposits from customers	-	205,562,678	1,108,575	4,947,913	1,439,371	4,818,954	-	217,877,491
Other liabilities	-	2,907,608	-	-	-	-	-	2,907,608
Subordinated loans	-	83,107	147,986	1,097,832	2,128,721	9,405,454	-	12,863,100
Total liabilities	**-**	**208,677,192**	**1,256,561**	**6,105,069**	**3,568,092**	**31,691,657**	**-**	**251,298,571**
Off-balance sheet liabilities	-	19,735	1,834,552	8,948,516	2,893,144	4,717,152	69,117	18,482,216

The table below presents the Bank's contractual undiscounted cash flows of the financial liabilities as at 31 December 2018:

	Past due	Within 1 month	1 – 3 months	3 – 6 months	6 –12 months	1–5 years	Over 5 years and undated	Total
	EUR	EUR	EUR	EUR	EUR	EUR	EUR	EUR
Debt securities	-	123,799	-	59,324	-	17,467,249	-	17,650,372
Deposits from customers	-	205,569,861	1,108,575	4,947,913	1,439,371	4,818,954	-	217,884,674
Other liabilities	-	2,907,608	-	-	-	-	-	2,907,608
Subordinated loans	-	83,107	147,986	1,097,832	2,128,721	9,405,454	-	12,863,100
Total liabilities	**-**	**208,684,375**	**1,256,561**	**6,105,069**	**3,568,092**	**31,691,657**	**-**	**251,305,754**
Off-balance sheet liabilities	**-**	19,735	1,834,552	8,948,516	2,893,144	4,721,709	69,117	18,486,773

31. Maturity analysis of assets and liabilities based on interest rate changes

The Group's assets and liabilities categorized by the earlier of contractual repricing or maturity dates as at as at 31 December 2019:

	Within one month EUR	1–3 months EUR	3–6 months EUR	6–12 months EUR	1–5 years EUR	Over 5 years EUR	Items not sensitive to the interest risk EUR	Total EUR
Assets								
Cash and balances with the Bank of Latvia	112,618,588	-	-	-	-	-	729,668	113,348,256
Balances due from banks	44,930,869	567,052	-	-	-	-	4,852,501	50,350,422
Loans and advances to customers	5,674,045	7,222,514	2,642,970	11,827,695	25,995,497	26,250	1,365,746	54,754,717
Financial assets at fair value through profit or loss	24,461,073	180,140	178,630	360,305	5,827,617	-	7,959	31,015,724
Equity instruments at fair value through other comprehensive income	-	-	-	-	-	-	412,205	412,205
Derivative financial instruments	-	-	-	-	-	-	42,340	42,340
Other assets	-	-	-	-	-	-	9,347,227	9,347,227
Total assets	**187,684,575**	**7,969,706**	**2,821,600**	**12,188,000**	**31,823,114**	**26,250**	**16,757,646**	**259,270,891**
Liabilities and equity								
Deposits from customers	137,940,728	17,129,639	21,416,783	7,811,371	37,610,389	-	50,143	221,959,053
Debt securities	-	-	-	-	17,803,098	-	93,322	17,896,420
Other liabilities	-	-	-	-	-	-	3,018,357	3,018,357
Corporate income tax	-	-	-	-	-	-	1,132	1,132
Subordinated loans	-	-	-	2,960,655	5,786,007	-	1,985	8,748,647
Total liabilities	137,940,728	17,129,639	21,416,783	10,772,026	61,199,494		3,164,939	251,623,609
Equity	-	-	-	-	-	-	36,373,840	36,373,840
Total liabilities and equity	**137,940,728**	**17,129,639**	**21,416,783**	**10,772,026**	**61,199,494**		**39,538,779**	**287,997,449**
Sensitivity of statement of financial position items to interest rate risk	49,743,847	(9,159,933)	(18,595,183)	1,415,974	(29,376,380)	26,250	(22,781,133)	(28,726,558)
As at 31 December 2018								
Total assets	**154,601,974**	**15,456,342**	**4,673,319**	**41,601,174**	**24,375,091**	**28,488**	**15,402,023**	**256,138,411**
Total liabilities and equity	**622,762**	**223,668**	**1,035,865**	**3,167,610**	**27,052,902**	**-**	**250,986,036**	**283,088,843**
Sensitivity of statement of financial position items to interest rate risk	153,979,212	15,232,674	3,637,454	38,433,564	(2,677,811)	28,488	(235,584,013)	(26,950,432)

31. Maturity analysis of assets and liabilities based on interest rate changes *(cont'd)*

The Bank's assets and liabilities categorized by the earlier of contractual repricing or maturity dates as at as at 31 December 2019:

	Within one month EUR	1–3 months EUR	3–6 months EUR	6–12 months EUR	1–5 years EUR	Over 5 years EUR	Items not sensitive to the interest risk EUR	Total EUR
Assets								
Cash and balances with the Bank of Latvia	112,618,588	-	-	-	-	-	729,668	113,348,256
Balances due from banks	44,930,869	567,052	-	-	-	-	4,852,501	50,350,422
Loans and advances to customers	5,674,045	11,765,599	2,642,970	11,827,695	25,995,497	26,250	1,365,746	59,297,802
Financial assets at fair value through profit or loss	24,461,073	180,140	178,630	360,305	5,827,617	-	7,959	31,015,724
Equity instruments at fair value through other comprehensive income	-	-	-	-	-	-	412,205	412,205
Derivative financial instruments	-	-	-	-	-	-	42,340	42,340
Other assets	-	-	-	-	-	-	7,002,138	7,002,138
Total assets	**187,684,575**	**12,512,791**	**2,821,600**	**12,188,000**	**31,823,114**	**26,250**	**14,412,557**	**261,468,887**
Liabilities and equity								
Deposits from customers*	138,394,851	17,129,639	21,416,783	7,811,371	37,610,389	-	50,143	222,413,176
Debt securities	-	-	-	-	17,803,098	-	93,322	17,896,420
Other liabilities	-	-	-	-	-	-	1,823,688	1,823,688
Corporate income tax	-	-	-	-	-	-	1,132	1,132
Subordinated loans	-	-	-	2,960,655	5,786,007	-	1,985	8,748,647
Total liabilities	138,394,851	17,129,639	21,416,783	10,772,026	61,199,494		1,970,270	250,883,063
Equity	-	-	-	-	-	-	35,427,208	35,427,208
Total liabilities and equity	**138,394,851**	**17,129,639**	**21,416,783**	**10,772,026**	**61,199,494**		**37,397,478**	**286,310,271**
Sensitivity of statement of financial position items to interest rate risk	49,289,724	(4,616,848)	(18,595,183)	1,415,974	(29,376,380)	26,250	(22,984,921)	(24,841,384)
As at 31 December 2018								
Total assets	**154,601,974**	**18,218,317**	**4,673,319**	**41,601,174**	**24,375,091**	**28,488**	**15,386,446**	**258,884,809**
Total liabilities and equity	**622,762**	**223,668**	**1,035,865**	**3,167,610**	**27,052,902**	**-**	**250,643,907**	**282,746,714**
Sensitivity of statement of financial position items to interest rate risk	153,979,212	17,994,649	3,637,454	38,433,564	(2,677,811)	28,488	(235,257,461)	(23,861,905)

32. Related party disclosures

Parties are considered to be related if one party has the ability to control the other party, are under common control or one exercises significant influence over the other party in making financial or operational decisions. Related parties are defined as shareholders, members of the Council and the Board, key management personnel of the Group and the Bank, their close relatives and companies in which they have a controlling interest as well as companies, where they have significant influence.

The parent company of the Group and the Bank is AB Pivdenny bank as it controls the operations of the Group and the Bank. The ultimate beneficiary of the Bank is Yuriy Rodin.

Transactions with related parties as at 31 December 2019 can be specified as follows:

	Parent company of the Bank	Entities owned by the Bank's shareholders	Subsidiary of the Bank	Other related parties
Total loans and advances to customers (contractual interest rate: 4-20%)	-	1,024,382	4,570,780	-
Correspondent account	10,291,789	-	-	-
Deposits from customers (contractual interest rate: 0.0%)	-	383,680	454,123	215,052
Subordinated loans (contractual interest rate: 7.0-8.5%)	-	3,249,787	-	-
Dividends paid	-	743,434	-	1,912,810

Income and expense from transactions with related parties in 2019 can be specified as follows:

	Parent company of the Bank	Entities owned by the Bank's shareholders	Subsidiary of the Bank	Other related parties
Interest income	243,373	66,707	157,362	284
Interest expense	-	(431,663)	-	(32,828)
ECL allowances	217	245,811	(27,031)	169
Fee and commission income	-	14,243	213	3,574
Other income	-	2,000	-	-
Fee and commission expense	6,513	-	-	-
Administrative and other operating expense	14,802	-	-	-

Off-balance sheet liabilities towards related parties as at 31 December 2019 can be specified as follows:

	Entities owned by the Bank's shareholders	Subsidiary of the Bank	Other related parties
Undrawn credit lines	-	-	5,900
Assets under management	1,315	-	4,888,987

Loans issued to and repaid by related parties in 2019 can be specified as follows:

	Parent company of the Bank	Entities owned by the Bank's shareholders	Subsidiary of the Bank	Other related parties
Issued to related parties	-	7	3,027,557	67,172
Repaid by related parties	-	819,378	1,235,000	67,172

Transactions with the Bank's parent company include the total amount of the current loans issued and repaid in 2019.

32. Related party *(disclosures)*

Transactions with related parties as at 31 December 2018 can be specified as follows:

	Parent company of the Bank	Entities owned by the Bank's shareholders	Subsidiary of the Bank	Other related parties
Total loans and advances to customers (contractual interest rate: 0-12%)	-	1,812,479	2,762,595	-
Correspondent account	10,058,882	-	-	-
Deposits from customers (contractual interest rate: 0.0%)	-	12,130,307	7,183	1,065,584
Subordinated loans (contractual interest rate: 7.0-8.5%)	-	8,292,127	-	-
Dividends paid	-	743,434	-	1,912,810

Income and expense from transactions with related parties in 2018 can be specified as follows:

	Parent company of the Bank	Entities owned by the Bank's shareholders	Subsidiary of the Bank	Other related parties
Interest income	737,320	100,379	106,800	210
Interest expense	-	650,778	-	-
Impairment allowances	456	(132,346)	694	182
Fee and commission income	-	15,501	186	1,665
Fee and commission expense	15,812	-	-	-
Administrative and other operating expense	18,149	-	600	-

Off-balance sheet liabilities towards related parties as at 31 December 2018 can be specified as follows:

	Entities owned by the Bank's shareholders	Subsidiary of the Bank	Other related parties
Undrawn credit lines	-	4,557	8,900
Assets under management	1,319	-	1,147

Loans issued to and repaid by related parties in 2018 can be specified as follows:

	Parent company of the Bank	Entities owned by the Bank's shareholders	Subsidiary of the Bank	Other related parties
Issued to related parties	25,720,960	-	261,443	57,319
Repaid by related parties	36,846,937	440,558	-	57,319

Transactions with the Bank's parent company include the total amount of the current loans issued and repaid in 2018.

32. Related party disclosures *(cont'd)*

Remuneration to the Board and Council of the Bank can be specified as follows:

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
Short-term benefits:				
- Salaries	802,051	796,891	610,220	610,220
- State statutory social insurance contributions	189,719	188,476	155,951	155,951
Total	**991,770**	**985,367**	**766,171**	**766,171**

33. Fair values of financial assets and liabilities

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The best evidence of fair value is quoted prices in an active market. An active market is one in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis. The Group and the Bank disclose information on fair values of assets and liabilities in such a way as to enable its comparison with their carrying amounts.

When determining fair values of assets and liabilities, the Group and the Bank use three hierarchical measurement levels of fair value:

Level 1 – Quoted prices in an active market;

Level 2 – Valuation techniques for which the input that is significant to the fair value measurement is observable in the market;

Level 3 – Other valuation techniques for which the input that is significant to the fair value measurement is unobservable.

Instruments within **Level 1** include financial instruments traded on the stock exchange.

Fair value for such financial instruments as financial assets at fair value through profit and loss is mainly determined based on publicly available quoted prices (bid price obtained from the Bloomberg system).

Instruments within **Level 2** include assets, for which no active market exists, such as over-the-counter (OCT) derivative financial instruments and currency swaps as well as balances on demand with the Bank of Latvia, amounts due from banks, financial assets at fair value through profit and loss, amounts due to banks and deposits from customers as well as other financial assets and liabilities.

The fair value of derivative financial instruments is based on discounted cash flow models with all parameters used (foreign currency exchange rate, interest rate) being observable in the market.

The fair value of cash and demand deposits with the Bank of Latvia is based on the estimated present value of discounted future cash flows. The discount rate applied is based on the interest rates prevailing in the market at the end of the year.

The fair value of balances due from banks is based on the estimated present value of discounted future cash flows. The discount rate applied is based on the interest rates prevailing in the market at the end of the year.

The fair value of deposits from customers is based on the estimated present value of discounted future cash flows. The discount rate applied is based on the interest rates prevailing in the market at the end of the year.

Notes to the financial statements *(cont'd)*

33. Fair values of financial assets and liabilities *(cont'd)*

The estimated fair value of other financial assets and liabilities is based on the estimated present value of discounted future cash flows. The discount rate applied is based on the interest rates prevailing in the market at the end of the year.

Level 3 instruments are available-for-sale financial assets as well as loans and subordinated debt.

In the reporting year, the fair value of available-for-sale financial instruments was based on an indicative price offer received from a potential buyer and which is considered to be the best estimate of the fair value.

The fair value of loans is based on the estimated present value of discounted future cash flows. Discount rate applied in the calculation is based on the interest rates prevailing in the market at the end of the year as adjusted for credit risk.

The fair value of the Subordinated loans is based on the estimated present value of discounted future cash flows. Discount rate applied in the calculation is based on the interest rate applied to the last transaction adjusted for the decline in the market rates observed in the respective period.

The fair value of debt securities is based on estimated present value of discounted future cash flows. Discount rate applied in the calculation is based on the interest rate applied to last transaction adjusted for the decline in the market rates observed in the respective period.

The carrying amounts of the Group's assets measured at amortized cost and their fair values can be specifies as follows:

	31.12.2019		31.12.2018	
	Carrying amount EUR	Fair value EUR	Carrying amount EUR	Fair value EUR
Assets measured at amortized cost				
Cash and balances with the Bank of Latvia	113,348,256	113,348,256	95,088,745	95,088,745
Balances due from banks	50,350,422	50,350,422	44,132,371	44,132,371
Loans to legal entities	53,140,384	58,040,044	82,304,655	89,094,220
Loans to private individuals, except for mortgages	1,520,026	1,709,039	3,039,727	3,387,513
Mortgages	94,307	110,468	154,097	182,449
Other financial assets	9,366,209	9,366,209	5,885,247	5,885,247
Total assets measured at amortized cost	**227,819,604**	**232,924,438**	**230,604,842**	**237,770,545**
Liabilities measured at amortized cost				
Deposits from customers	221,959,053	222,025,911	217,830,443	219,245,093
Debt securities	17,896,420	17,896,420	17,558,810	17,558,810
Subordinated loans	8,748,647	8,846,348	11,207,357	11,353,625
Other financial liabilities	2,052,786	2,052,786	2,932,204	2,932,204
Total liabilities measured at amortized cost	**250,656,906**	**250,821,465**	**249,528,814**	**251,089,732**

Notes to the financial statements *(cont'd)*

33. Fair values of financial assets and liabilities *(cont'd)*

The carrying amounts of the Bank's assets measured at amortized cost and their fair values can be specifies as follows:

	31.12.2019		31.12.2018	
	Carrying amount EUR	Fair value EUR	Carrying amount EUR	Fair value EUR
Assets measured at amortized cost				
Cash and balances with the Bank of Latvia	113,348,256	113,348,256	95,088,745	95,088,745
Balances due from banks	50,350,422	50,350,422	44,132,371	44,132,371
Loans to legal entities	57,683,469	62,781,645	85,066,630	91,972,181
Loans to private individuals, except for mortgages	1,520,026	1,709,039	3,039,727	3,387,513
Mortgages	94,307	110,468	154,097	182,449
Other financial assets	7,021,120	7,021,120	5,869,670	5,869,670
Total assets measured at amortized cost	**230,017,600**	**235,320,950**	**233,351,240**	**240,632,929**
Liabilities measured at amortized cost				
Deposits from customers	222,413,176	222,480,034	217,837,626	219,252,277
Debt securities	17,896,420	17,896,420	17,558,810	17,558,810
Subordinated loans	8,748,647	8,846,348	11,207,357	11,353,625
Other financial liabilities	858,117	858,117	2,907,608	2,907,608
Total liabilities measured at amortized cost	**249,916,360**	**250,080,919**	**249,511,401**	**251,072,320**

Notes to the financial statements *(cont'd)*

33. Fair values of financial assets and liabilities *(cont'd)*

The Group's assets by fair value hierarchy levels (at carrying amounts) can be specified as follows:

	31.12.2019			31.12.2018		
	Level 1 EUR	Level 2 EUR	Level 3 EUR	Level 1 EUR	Level 2 EUR	Level 3 EUR
Assets measured at fair value						
Derivative financial instruments	-	42,340	-	-	-	-
Available-for-sale financial assets	-	-	412,205	-	-	284,083
Financial assets at fair value through profit or loss	29,799,307	1,216,687	-	23,976,121	1,273,367	-
Total assets measured at fair value	**29,799,307**	**1,259,027**	**412,205**	**23,976,121**	**1,273,367**	**284,083**
Assets for which fair value is disclosed						
Cash and balances with the Bank of Latvia	-	113,348,256	-	-	95,088,745	-
Balances due from banks	-	50,350,422	-	-	44,132,371	-
Loans and advances to customers	-		54,754,717	-	-	85,498,479
Other financial assets	-	9,366,209	-	-	5,885,247	-
Total assets for which fair value is disclosed	**-**	**173,064,887**	**54,754,717**	**-**	**145,106,363**	**85,498,479**
Liabilities measured at fair value						
Derivative financial instruments	-	-	-	-	-	-
Total liabilities measured at fair value	**-**	**-**	**-**	**-**	**-**	**-**
Liabilities for which fair value is disclosed						
Deposits from customers	-	221,959,053	-	-	217,830,443	-
Debt securities	-	-	17,896,420	-	-	17,558,810
Subordinated loans	-	-	8,748,647	-	-	11,207,357
Other financial liabilities	-	2,052,786	-	-	2,932,204	-
Total liabilities for which fair value is disclosed	**-**	**224,011,839**	**26,645,067**	**-**	**220,762,647**	**28,766,167**

33. Fair values of financial assets and liabilities *(cont'd)*

The Bank's assets by fair value hierarchy levels (at carrying amounts) can be specified as follows:

		31.12.2019			31.12.2018	
	Level 1 EUR	Level 2 EUR	Level 3 EUR	Level 1 EUR	Level 2 EUR	Level 3 EUR
Assets measured at fair value						
Derivative financial instruments	-	42,340	-	-	-	-
Available-for-sale financial assets	-	-	412,205	-	-	284,083
Financial assets at fair value through profit or loss	29,799,307	1,216,687	-	23,976,121	1,273,367	-
Total assets measured at fair value	**29,799,307**	**1,259,027**	**412,205**	**23,976,121**	**1,273,367**	**284,083**
Assets for which fair value is disclosed						
Cash and balances with the Bank of Latvia	-	113,348,256	-	-	95,088,745	-
Balances due from banks	-	50,350,422	-	-	44,132,371	-
Loans and advances to customers	-		59,297,802	-	-	88,260,454
Other financial assets	-	7,021,120	-	-	5,869,670	-
Total assets for which fair value is disclosed	**-**	**170,719,798**	**59,297,802**	**-**	**145,090,786**	**88,260,454**

Liabilities measured at fair value						
Derivative financial instruments	-	-	-	-	-	-
Total liabilities measured at fair value	**-**	**-**	**-**	**-**	**-**	**-**
Liabilities for which fair value is disclosed						
Deposits from customers	-	222,413,176	-	-	217,837,626	-
Debt securities	-	-	17,896,420	-	-	17,558,810
Subordinated loans	-	-	8,748,647	-	-	11,207,357
Other financial liabilities	-	858,117	-	-	2,907,608	-
Total liabilities for which fair value is disclosed	**-**	**223,271,293**	**26,645,067**	**-**	**220,745,234**	**28,766,167**

34. Subordinated loans

Subordinated loans as at 31 December of 2019 and 31 December 2018 can be specified as follows:

	31.12.2019 Group EUR	%	31.12.2019 Bank EUR	%	31.12.2018 Group EUR	%	31.12.2018 Bank EUR	%
Fortum Trade Services LTD (maturity 2019-2021)	-	-	-	-	7,855,348	7,00-8,50	7,855,348	7,00-8,50
Sky Investment Holding SIA (maturity 2021)	2,492,988	8,00	2,492,988	8,00	-	-	-	-
Heshvan Limited (maturity 2020-2021)	2,103,918	8,00-8,50	2,103,918	8,00-8,50	2,064,228	8,00-8,50	2,064,228	8,00-8,50
Milandale Limited (maturity 2021)	-	-	-	-	436,778	8,00	436,778	8,00
Ronby Invest LLP (maturity 2020-2021)	1,391,635	8,00-8,50	1,391,635	8,00-8,50	-	-	-	-
Villa Flora SIA (maturity 2021)	756,800	8,00	756,800	8,00	-	-	-	-
UK Industries Group LTD (maturity 2020-2021)	690,766	8,00-8,50	690,766	8,00-8,50	-	-	-	-
Maxiplan L.P (maturity 2020)	-	-	-	-	370,563	8,50	370,563	8,50
Marks Bekkers (maturity 2020)	445,176	8,00	445,176	8,00	-	-	-	-
Zhelizna Viktorija (maturity 2020)	377,687	8,50	377,687	8,50	-	-	-	-
Igors Chudenkov (maturity 2020)	373,953	8,50	373,953	8,50	366,899	8,50	366,899	8,50
Andrejs Volodin (maturity 2020)	115,724	8,50	115,724	8,50	113,541	8,50	113,541	8,50
Total subordinated loans	**8,748,647**		**8,748,647**		**11,207,357**		**11,207,357**	

35. Assets under management

Assets under management are securities and other customer assets acquired under trust agreements.

	31.12.2019 Group EUR	31.12.2019 Bank EUR	31.12.2018 Group EUR	31.12.2018 Bank EUR
Legal entities:				
- non-residents	62,974,825	62,974,825	68,836,200	68,836,200
Private individuals:				
- residents	-	-	216,624	216,624
- non-residents	5,202,377	5,202,377	457,519	457,519
Total	**68,177,202**	**68,177,202**	**69,510,343**	**69,510,343**

36. Return on equity and return on assets

	31.12.2019 Group	31.12.2019 Bank	31.12.2018 Group	31.12.2018 Bank
Return on equity (ROE) (%)	10,31%	8,67%	15,52%	15,66%
Return on assets (ROA) (%)	1,39%	1,15%	1,78%	1,80%

Both ratios are calculated according to the FCMC regulations on the basis of annual averages month by month. ROE is calculated as annualized net profit for the reporting period divided by the average of total equity. Return on average assets (ROA) is calculated as annualized net profit for the reporting period divided by the average of total assets.

37. Going concern

The series of events that started in 2018 with the suspension of the operations of ABLV Banka have significantly affected the banking sector in Latvia; as a result Latvian banks had to review their business models and considerably change business development plans.

In May 2018, amendments to the AML/CFT Law came into force restricting the service provision to part of the shell companies. In August 2018, the Moneyval report on the valuation of Latvian financial system was published outlining its shortcomings. Throughout the year 2019, information about the possible involvement of Baltic branches of 'Scandinavian' banks in money laundering schemes was widely communicated. On 15 August 2019, the operations of PNB banka were suspended, and on 12 September PNB banka was declared insolvent by Riga City Vidzeme District Court. In the second half of 2019, a new Head of the FCMC and a new President of the Bank of Latvia were assigned appointed.

In the light of the above mentioned events, in 2019 the overhaul of the financial sector in Latvia continued with the aim of significantly improving the transparency of the financial sector by stimulating active tackling of money laundering. Already since 2018, an active ML/FTP risk management process has been taking place which continued throughout the year 2019. During that period a number of significant measures were taken for achieving the objectives of the financial sector reform, e.g., prohibition to provide services to high-risk shell companies as well as to settle real estate transactions in cash; measures were taken to improve access to information on ultimate beneficiaries; regulation on ensuring compliance with national and international sanctions was improved; and the ability of the supervisory bodies of the financial sector to fight against financial crime was strengthened at an institutional level. In 2019, banks continued improving their risk control systems and thoroughly analyzing and revising their customer base.

Notwithstanding that, the impact of 2018-2019 events on the overall activities of the banking system was not critical, those Latvian credit institutions whose operations so far had mainly been based on foreign customer service had to adapt to the new circumstances and change their business models. This type of banks has already been working on it since spring 2018. The public information on the involvement of 'Scandinavian' banks in money laundering schemes communicated in 2019 had also a

37. Going concern *(cont'd)*

material impact on the operational strategy of the banks of the said segment. Too precautionary approach to the customer base, massive de-risking measures focused on industries and customer types in whole rather than on particular customers considerably limited the availability of the 'Scandinavian' banking services to a number of Latvian enterprises. This provides Latvian business an incentive to look more actively for cooperation possibilities with local banks, minimizing the risk of incidental account closing and choosing to work with several banks simultaneously. All these events supported the business transformation processes previously initiated by the Bank and provided additional opportunities for its business development in Latvia.

In April 2019, the Bank's Development Strategy 2019-2022 was approved which is a specified version of the previous development strategy of the Bank aimed at development of a sound and effective specialized European bank that offers professional advice and a range of products and services according to market demand in lending and corporate finance areas. The Bank's products are oriented to legal entities – Latvian/EU SMEs, as well as to private individuals – employees, managers and owners of the SMEs serviced by the Bank.

The new strategic approach is based on key driving factors of implementing the new business model, which will be the Bank's priority for achieving its goals. One of the main transformation driving factors is enhanced competency in providing lending services in local market, which is achieved by establishing a competent and experienced team, development of new lending products as well as development of a new lending and interest rate policy. No less important driving factor is related to the brand and image development of the Bank whereby the Bank defines its new brand as well as Marketing and Communication Strategy subject to the business model. In order to avoid larger expenditure than necessary and to ensure that the Bank maintains its profitability, the strategic approach requires maximum adaptation of the existing resources and technologies to the emerging needs.

If the events of 2018 required considerable efforts by the Bank to define its role meeting the new conditions of the banking market under transformation, in 2019 work was done on a systematic basis. The focus was on entering new market segments, revision of standard products and business approaches as well as the introduction of new products/services oriented on new non-resident customer groups.

In 2019, deposits from customers increased by EUR 4,6 million and at the end of 2019 totaled EUR 222,4 million, by EUR 22,9 million exceeding the Bank's management projections made during the development and approval phases of the Bank's Development Strategy in spring 2019. As a result of a more prudent lending policy, in 2019 new loans of EUR 29.4 million were issued, an increase of 41.3% against the year 2018, and loans of EUR 70.5 million were repaid, including the recovery of non-performing loans and written-off loans of EUR 8,2 million. Accordingly, the total loan portfolio decreased by 36%. Notwithstanding such an overall portfolio dynamic, the Bank maximally maintained profitability of its basic product due to the increased annual effective interest rate – the interest income fell only by 10.2% and reached EUR 6.3 million. As at 31 December 2019, the total loan portfolio amounted to EUR 71,2 million. In the reporting year, ECL allowances decreased by 47%. In general, the year 2019 was closed with a positive result – the Bank's net profit reached EUR 2.99 million, and at the end of 2019 return on equity (ROE) and return on assets (ROA) ratios were 8.67% and 1.15% respectively.

37. Going concern *(cont'd)*

In 2020, the Bank plans to improve the uptake of its new local and EU market-oriented strategy, which will lead to a considerable increase in the resident loan portfolio and income as well as deposits from local customers and account turnover. In 2020, the Bank expects a change in deposits from customers (settlement accounts and deposits) within the indicative limit of EUR 151 million. The activities of the Bank's sales marketing team in 2020 will result in increasing the share of Latvian loan portfolio in the Bank's total loan portfolio with the share of the CIS-related loan portfolio gradually decreasing.

In line with its Development Strategy, in 2019, the Bank finalized the preparation for attracting deposits from customers through deposit platforms and received the first deposits from German residents – private individuals. The first deposits were placed with the Bank on 2 January 2019; as at 31 December 2019, the bank had attracted deposits total EUR 34.8 million with a maturity from 3 to 24 months. The Bank expects that the amount of deposits attracted in 2020 through the deposit platform will gradually decrease and that at the end of 2020 it will reach about EUR 19 million.

In December 2019, the Supervisory Council of the Bank approved the IT Development Strategy aimed at introducing a number of new technological solutions and development of the existing technologies of the Bank. In 2020, the Bank plans to finalize several earlier projects started in 2018 as well as new projects of strategic importance for the transformation of the Bank's business model. The customers will be offered advanced Mobile Banking application of Internet bank and in the following three years also a modern technology-based Internet bank.

By the end of the second quarter of 2020, the Bank plans to review, get approved by the Supervisory Council and submit to the FCMC the new Development Strategy 2020-2024 which would include a specified development scenario for the next four years taking into account both the results of the Bank's transformation in 2019 and its management's vision about opportunities for further development on Latvian and EU markets.

According to the strategy and budget, in 2020 the share of interest income from Latvian and EU customers will grow, while interest income will generally decrease by 9% against the year 2019; whereas the fall in fee and commission income (by 3% against the year result of 2019), related to the overall reduction of the customer base, will be compensated by smaller interest expense (decrease by 12%) and fee and commission expense (decrease by 5%). After the revision of administrative expense in 2019, the administrative expenditure part of the budget 2020 will decrease by 9% against the year 2019. In line with the budget 2020, the Bank will close the year with a net profit of about EUR 1,13 million.

The transformation processes both at the Bank itself and in Latvian banking sector give rise to a material uncertainty which may cast significant doubt on the Group and Bank's ability to continue as a going concern and, therefore, on their ability to realize their assets and discharge their liabilities in the normal course of business. However, the experience during 2019 and good financial performance as well as the prudent budget for the year 2020 show the Bank's ability to adapt to changes and proceed with the initiated transformation processes. The Group and Bank's management does not believe that the changes in the Bank's business strategy as well as further improvements in Latvian banking sector could negatively affect the Group and Bank's business model and further development.

In the third quarter of 2019, the FCMC performed an inspection at the Bank on the prevention of money laundering and terrorist and proliferation financing and the sanctions risk management for the period from January 01, 2017 to June 30, 2019.

37. Going concern *(cont'd)*

At the date of signing these financial statements, the final results of the FCMC inspection had not yet been received. During the inspection, the Bank submitted to the FCMC inspection team all required explanations and documents; at the date of signing these financial statements, no additional questions concerning the inspection had been received which gives rise to uncertainty regarding the further process development. In recent years, it has been noted in the bank sector of Latvia that penalty sanctions have been rather often applied to banks after such FCMC inspections, wherewith the possibility of a penalty cannot be fully excluded. Pursuant to Article 196 (2) of the Law on Credit Institutions of the Republic of Latvia and Article 78 (3) (1) of the Law on the Prevention of Money Laundering and Terrorism and Proliferation Financing, for breach of the AML regulations on credit institution may be imposed fine up to 10 percent of its total annual turnover according to the last approved financial statement, prepared, approved and audited. The law provides that if 10 percent of the total annual turnover is less than EUR 5,000,000, the supervisory and control body is entitled to impose fines of up to EUR 5,000,000. The Bank's management believes that the internal control system established at the Bank in the area of AML/CFTP and sanctions (hereinafter – ICS) complies with applicable regulatory requirements.

The Bank's management confirms that the outcome of the said inspection will not affect the Bank's ability to honor their commitments towards its customers and partners. The Bank's management believes that the Bank strictly complies with the applicable laws and regulations, including those governing the prevention of money laundering, breaches of sanctions or attempts of their circumvention and terrorist and proliferation financing.

The Bank continually enhances and improves its ICS facilitating/ensuring customer and customer transaction monitoring in compliance with technological and regulatory requirements and preventing the execution of transactions contradicting the internal regulations of the Bank and KYC/KYCP policies or with characteristics of a suspicious transaction, e.g., when circumstances that can indicate a possible breach of sanctions or circumvention of them are identified. Bank will carefully consider the results of the FCMC inspection and observations of the inspecting team in the ICS further development.

The Bank's shareholders have provided written confirmations regarding their support to the Bank in the process of transition to the new business model and readiness to provide financial support; if needed, to comply with the capital and liquidity requirements until 31 December 2020.

38. Subsequent events

Except as stated below, as of the last day of the reporting year until the date of signing these financial statements there have been no other events requiring adjustment of or disclosure in the financial statements or notes thereto.

In February 2020, FCMC initiated the regular on-site inspection at the Bank. The aim of the inspection is to assess the Bank's corporate management, strategic planning, lending, and credit risk management processes. The Bank actively cooperates with the FCMC audit group and has submitted all the necessary documents. It is planned that the inspection process will continue until the end of March 2020.

Aleksandrs Jakovļevs
Chairman of the Board

Yuriy Rodin
Chairman of the Council

Riga, 04 March 2020