JSC “REGIONALA INVESTICIJU BANKA”

ANNUAL REPORT FOR THE YEAR ENDED 31 DECEMBER 2013

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JSC "Regionala investiciju banka"

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Report of the Management

2013 was a year of successful development for JSC “Regionala investiciju banka” (hereinafter referred to as “Bank”), during which the number of Customers increased by 19.4% in comparison with 2012. In 2013, profit from the Bank’s principal activity was EUR 945,803; however, in order to improve the quality of assets, the Bank has created large bad debts reserves of EUR 8.37 million.

Overall economic situation

Despite of global economy growth being rather slow, as well as despite significant uncertainty on the future development trends in the key global economy players, Latvian economy in past three years has shown remarkable growth rates.

GDP dynamics of past three years proves that economy growth has been steady and there are no steep increases or decreases in GDP trend across quarters. This results in optimistic future outlook, as none of prior years’ indicators are pointing to the overheating of economy and allow estimating that, even in case the state may not provide for such rate of increase in GDP in the future, possibilities of significant downturns are rather insignificant.

Key source of increase in Latvian economy in 2013 was significant increase in trading. Retail in second quarter of 2013 grew by 6.3%. This is mainly explained by increasing wealth of households and increasing consumer satisfaction indices. Decline of unemployment rates and upcoming accession of Latvia to the Eurozone further strengthened belief of society in positive development of economy in the future and despite the willingness to create savings, it boosted household consumption rates.

Estimating future developments in Latvian economy, it should be noted that export power retains its significance. Up till now due to internal devaluation and increase of productivity, goods producers have regained their competitiveness and managed to attract attention of foreign customers in a successful manner.

In 2013 Latvian financial sector was showing tendencies similar to 2012 with banks’ assets remaining stable. Liquidity in banking sector is still above legal requirements of 30%. Latvian banks are very well capitalised, with capital adequacy being around 18%. However negative trend in decline of total issued loans continues, thus slowing down increase in profitability and incomes of the banks. Despite loan issuance has not reached optimum levels and banks keeping to their conservative positions, future provides for optimistic outlooks and expectations. The fact that credit quality of banking loan portfolios is increasing also supports optimism in predicting cessation of decline in banking loan portfolio at the end of the year with succeeding positive growth. As a result, this may increase revenue and profitability of banks and their return to the pre-crisis levels.

Unlike Latvia in 2013 Ukraine experienced decline in economic activity. Decline in economic activity is mainly explained by adverse situation in the state export markets, especially slow growth of European Union economies, which are major trading partners of the state. Major threats to successful growth of the economy are relatively high current account deficit, significant external debt and high price for its servicing.

Ukrainian financial sector alike to the country economy is experiencing hard times. Quality of bank assets is still poor and problematic loans comprise around 35% of the loan portfolios, the same as in 2012. Despite total banking sector showing positive profit tendencies, revenues and interest rates are low thus making banking sector risky and decreasing possibilities for attraction of resources in foreign markets. Further decline in investments, which are so needed for the development of Ukrainian economy, is caused by current economic and political instability in the country.

Report of the Management (continued)

Performance of the Bank during the Reporting Period

Due to the fact that in 2013 the Bank launched a new service to its Customers, i.e. Trust Transactions, a part of funds from the Bank's balance sheet was moved to off-balance and that is why the Bank's assets decreased by 6.8% in comparison with the end of the previous year and were EUR 451.64 million as at 31 December 2013. The total funds of the Bank's Customers accounted for on balance sheet and off-balance have increased by 10.3% in comparison with 2012. The deposit portfolio, taking into account the Trust Transactions, has decreased in numerical terms by 8.31% and was EUR 397.79 million as at 31 December 2013.

Also in 2013, the Bank continued to improve the quality of the credit portfolio therefore the amount of the credit portfolio decreased by 32.6% in comparison with 2012 and was EUR 69.85 million as at 31 December 2013.

On 1 January 2014, Latvia joined the Eurozone, and euro is now the official currency of Latvia. In order to ensure a successful implementation of euro, in the second half of 2013, the Bank successfully completed the euro implementation project which required large human, IT and financial resources.

On 8 January 2013, a new member of the Board was elected – Vice-Chairman of the Board – Aleksandrs Kovalskis, who is managing all structural units related to servicing of Customers. One of the main tasks of the new Vice-Chairman of the Board is to improve Customer services and increase the number of Customers. At the end of the year, the Bank was serving 4839 Customers, and, in comparison with the results of 2012, the number of Customers in 2013 has increased by 19.4%.

In 2013, the Bank started an ambitious expansion of the network of correspondent banks, and over the year the Bank opened several new correspondent accounts in China, Turkey and Russia. By expanding the network of correspondent banks, the Bank has improved the quality of servicing transfers ensuring efficient and fast delivery of Customer funds to their destination. This innovation is also appreciated by our Customers and the number of outgoing transfers in 2013 increased by 11.7% in comparison with 2012.

Continuing the positive trend of the previous years, the amount and number of the documentary operations services increased also in 2013. In comparison with 2012, turnover of the money flow of letters of credit and collections increased by 20% and was EUR 117.2 million. Moreover, income from servicing the documentary operations transactions increased by 16 % in comparison with 2012 and was EUR 530.1 thousand.

In comparison with 2012, the number of payment cards in 2013 increased by 17.1%, while the turnover of the payment cards in 2013 increased by 8% and was EUR 21.97million. Towards the end of 2013, the Bank finalised the implementation of the acceptance service of payment cards, and, as of 2014, the Bank offers its Customers an option to accept MasterCard, Maestro, Visa and Visa Electron payment cards at their points of sale in Latvia. The Bank has also received a cross-border licence of MasterCard and VISA for the acceptance of payment cards on the Internet, which allows offering this service to e-commerce traders not only in Latvia, but in the whole of Europe.

In September 2013, the Finance and Capital Market Commission (FCMC) determined the individual capital requirement of 13.9% which the Bank has complied with. The individual liquidity ratio requirement set by FCMC was 60%, and the Bank's average liquidity ratio in 2013 was 79.1%.

In the second half of 2013, the Bank launched an implementation project of a new Internet bank, which had to be completed within a very short period of time. The new IT platform for the Internet bank was implemented in the beginning of 2014, however, the quality of functioning was not satisfactory at the time of implementation therefore we are currently continuing a swift work of improvement of the new Internet bank.

In the field of IT, the Bank has also modernised several systems and software. The operation speed and creation of statements of the Bank's accounting system have been improved, as well as accounting module for gold has been developed. The Bank's record-keeping software has been adjusted to using "e-signature", and several document management processes have been automated. Also, the single system for registering and administering the IT management processes has been updated, and new, functionally convenient modules have been introduced for the purposes of work of the Money Laundering Prevention Department.

Report of the Management (continued)

In 2013, the Bank's organisational structure was improved and three new structural units – Monitoring Section, Real Estate Section and Safety Control Section – were established. During the year, the number of the Bank's employees increased by 8 people, and the total number of employees on 31 December 2013 was 137.

Plans and Prospects for the Year 2014

In 2014 and henceforth, the Bank will continue to increase the number of Customers especially focusing on regions such as Russia and Kazakhstan.

In the field of services and product development, the Bank has set the following products as its priorities: Financial Services, E-Commerce and Internet bank. The new IT platform of the Internet bank will allow developing its functionality and offer the option to the Customers to receive all Bank's services remotely.

By analysing the Customer needs and behaviour in the transfer segment, also in 2014, the Bank will continue to expand the network of correspondent banks in order to improve transfer efficiency and to ensure fast transfers of funds.

Haralds Abolins
Chairman of the Board, President

Iurii Rodin
Chairman of the Council

Riga, 21 March 2014

THE SUPERVISORY COUNCIL AND THE BOARD OF DIRECTORS OF THE BANK

As at 31 December 2013 and as at the date of signing the accounts:

The Council

		Date of appointment
Iurii Rodin	Chairman of the Council	Re-elected – 24.02.2012
Mark Bekker	Deputy Chairman of the Council	Re-elected – 24.02.2012
Dmitrijs Bekkers	Member of the Council	Re-elected – 24.02.2012
Alla Vanetsyants	Member of the Council	Re-elected – 24.02.2012
Iryna Buts	Member of the Council	Re-elected – 24.02.2012

The Board

Haralds Abolins	Chairman of the Board and President	Re-elected – 28.06.2012
Olexandr Kovalsky	Deputy Chairman of the Board	08.01.2013
Daiga Muravska	Member of the Board	Re-elected – 28.06.2012

STATEMENT OF RESPONSIBILITY OF THE MANAGEMENT

The Supervisory Council and the Board of Directors (hereinafter - the Management) of the Bank are responsible for the preparation of the financial statements of the Bank.

The financial statements on pages 10 to 57 are prepared in accordance with the source documents and present fairly the financial position of the Bank as at 31 December 2013 and the results of its operations and cash flows for the reporting year 2013.

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 judgements 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, Bank of Latvia and other legislation of the Republic of Latvia applicable for credit institutions.

Haralds Abolins Chairman of the Board, President	Iurii Rodin Chairman of the Council

Riga, 21 March 2014

pwc

Translation from Latvian original*

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of AS Reģionālā Investīciju banka

Report on the Financial Statements

We have audited the accompanying financial statements on pages 10 to 57 of AS Reģionālā Investīciju banka (the "financial statements"), which comprise the statement of financial position as of 31 December 2013 and the statements of other comprehensive income, changes in equity and cash flows for the year then ended, and notes comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with 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.

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the AS Reģionālā Investīciju banka as of 31 December 2013, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

Emphasis of Matter – Operating Environment

We draw your attention to Note 32 to the financial statements. The operations of the Bank, and those of other entities in Ukraine, have been affected and may continue to be affected for the foreseeable future, by the continuing uncertainties in Ukraine. Our opinion is not qualified in respect of this matter.

Report on Other Legal and Regulatory Requirements

We have read the Management Report set out on pages 3 to 5 and did not identify material inconsistencies between the financial information contained in the Management Report and that contained in the accompanying financial statements.

PricewaterhouseCoopers SIA
Certified audit company
Licence No. 5

Ilandra Lejiņa
Member of the Board

Terēze Labzova
Certified auditor in charge
Certificate No. 184

Riga, Latvia
21 March 2014

* This version of our report is a translation from the original, which was prepared in Latvian. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation.

Statement of Comprehensive Income for the year ended 31 December 2013

	Notes	2013 LVL	2012 LVL
Interest income	5	13,214,738	14,191,474
Interest expense	5	(5,901,065)	(8,793,542)
Net interest income		**7,313,673**	**5,397,932**
Provisions for loan impairment	11	(5,880,431)	(3,200,189)
Net interest income after provision for loan impairment		**1,433,242**	**2,197,743**
Fee and commission income	6	4,783,147	3,997,785
Fee and commission expense	6	(1,097,586)	(1,228,464)
Net fee and commission income	6	**3,685,561**	**2,769,321**
Profit on securities trading, net		16,740	120
Profit/ (loss) from revaluation of securities at fair value through profit and loss account		(201,057)	553,481
Profit/ (loss) on derivative financial instruments revaluation		110,419	(97,870)
Profit on operation with foreign exchange, net		795,665	762,104
Profit/ (loss) from revaluation of foreign exchange, net		(243,436)	65,887
Other operating income		399,929	589,261
Administrative expense	7	(4,221,875)	(4,204,325)
Amortisation and depreciation charge	13, 14	(182,809)	(225,011)
Other operating expense		(89,372)	(67,184)
Profit from decrease in provisions		-	26,475
Profit before income tax		**1,503,007**	**2,370,002**
Income tax expense	8	-	-
Amount of tax paid abroad	8	(858,814)	(816,577)
Deferred income tax	8	20,521	(13,577)
Net profit for the year		**664,714**	**1,539,848**
Total comprehensive income for the year attributable to the owners of the Bank		**664,714**	**1,539,848**

The financial statements on pages 10 to 57 have been approved by the Supervisory Council and the Board of Directors of the Bank and signed on their behalf by:

Haralds Abolins
Chairman of the Board, President

Iurii Rodin
Chairman of the Council

Riga, 21 March 2014

The accompanying notes on pages 14 to 57 are an integral part of these financial statements.

Statement of Financial Position as at 31 December 2013

	Notes	31.12.2013 LVL	31.12.2012 LVL
Assets			
Cash and balances with the Bank of Latvia	9	23,088,266	44,440,857
Balances due from banks	10	222,195,264	207,381,802
Loans and advances to customers	11	49,090,287	72,830,308
Financial assets at fair value through profit or loss	12	16,555,553	13,793,922
Derivative financial instruments	20	165,898	112,637
Intangible assets	13	162,706	148,716
Property and equipment	14	192,687	225,108
Other assets		3,145,387	1,477,816
Deferred expenses		65,111	68,459
Deferred income tax asset	19	13,572	-
Corporate income tax	30	-	-
Total assets		**314,674,731**	**340,479,625**
Liabilities			
Balances due to banks	16	47,705	1,690,733
Balances due to customers	15	279,564,913	304,888,231
Derivative financial instruments	20	100,061	157,219
Other financial liabilities	17	434,416	2,968,887
Deferred income and accrued expenses	18	540,710	661,491
Deferred income tax liability	19	-	6,949
Subordinated loan	31	7,639,818	4,423,721
Total liabilities		**288,327,623**	**314,797,231**
Equity			
Share capital	21	22,725,000	22,725,000
Retained earnings		2,957,394	1,417,546
Comprehensive income for the year		664,714	1,539,848
Total equity		**26,347,108**	**25,682,394**
Total liabilities and equity		**314,674,731**	**340,479,625**
Commitments and contingent liabilities			
Contingent liabilities	22	2,399,357	6,016,694
Financial commitments	22	26,030,282	19,170,535
Assets under management		58,160,424	

The financial statements on pages 10 to 57 have been approved by the Supervisory Council and the Board of Directors of the Bank and signed on their behalf by:

Haralds Abolins
Chairman of the Board, President

Iurii Rodin
Chairman of the Council

Riga, 21 March 2014

The accompanying notes on pages 14 to 57 are an integral part of these financial statements.

Statement of Changes in Equity for the year ended 31 December 2013

	Paid-in share capital	Retained earnings	Total
	LVL	LVL	LVL
Balance as at 31 December 2011	**11,125,000**	**1,417,546**	**12,542,546**
Increase in paid-in share capital	11,600,000	-	11,600,000
Comprehensive income for the year	-	1,539,848	1,539,848
Balance as at 31 December 2012	**22,725,000**	**2,957,394**	**25,682,394**
Comprehensive income for the year	-	664,714	664,714
Balance as at 31 December 2013	**22,725,000**	**3,622,108**	**26,347,108**

The accompanying notes on pages 14 to 57 are an integral part of these financial statements.

Statement of Cash Flows for the year ended 31 December 2013

	Notes	2013 LVL	2012 LVL
Cash flows from operating activities			
Interest received		11,418,462	12,526,015
Interest paid		(6,170,296)	(9,284,024)
Fees and commission received		4,783,147	3,997,785
Fees and commission paid		(1,097,586)	(1,228,464)
Income on securities trading		16,740	120
Income on foreign exchange		795,665	762,104
Other operating income		399,929	589,261
Personnel expenses paid		(2,452,116)	(2,482,508)
Administrative and other operating expenses		(1,859,131)	(1,789,001)
Income tax paid		(858,814)	(816,577)
Cash flows generated from operating activities before changes in operating assets and liabilities		**4,976,000**	**2,274,711**
Changes in operating assets and liabilities			
Net increase of securities at fair value through profit and loss account		(2,902,295)	(3,968,279)
Net increase of balances due from banks		(32,313,465)	(12,430,265)
Net decrease of loans and advances to customers		18,504,948	7,979,277
Net increase of other assets		(1,664,223)	(457,740)
Net (decrease)/ increase of balances due to customers		(18,117,330)	96,416,340
Net (decrease)/ increase in other liabilities		(2,947,655)	1,877,054
Net cash and cash equivalents (used in)/ generated from operating activities		**(34,464,020)**	**91,691,098**
Cash flows from investing activities			
Purchase of intangible assets		(102,091)	(15,099)
Purchase of fixed assets		(62,287)	(34,575)
Net cash and cash equivalents used in investing activities		**(164,378)**	**(49,674)**
Cash flows from financing activities			
Proceeds from share issue		-	11,600,000
Subordinated loan received		3,508,500	7,587,000
Repayments of subordinated loan		-	(8,191,830)
Net cash and cash equivalents generated from financing activities		**3,508,500**	**10,995,170**
Effect of exchange rates on cash and cash equivalents		(3,285,066)	(5,099,974)
Net (decrease) / increase in cash and cash equivalents		**(34,404,964)**	**97,536,620**
Cash and cash equivalents at the beginning of the year	**23**	227,037,573	129,500,953
Cash and cash equivalents at the end of the year	**23**	**192,632,609**	**227,037,573**

The accompanying notes on pages 14 to 57 are an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 INCORPORATION AND PRINCIPAL ACTIVITIES

JSC "Regionala investiciju banka" (hereinafter – the Bank) provides financial services to corporate clients and individuals. The Bank established its representative office in Odessa, Ukraine in 2005 and representative office in Dnepropetrovsk, Ukraine in 2007. In the beginning of 2009 the Bank has established new representative office in Kiev, Ukraine. Furthermore, in 2010 the Bank has established its representative office in the capital of Belgium – Brussels. The Bank has no subsidiaries and branches apart from the mentioned above.

The Bank is a joint-stock company incorporated and domiciled in Riga, Republic of Latvia. It was registered within Commercial Register on 28 September 2001.

The legal and basic address of the Bank is:
2 J. Alunana Street,
LV-1010, Riga,
Latvia

These financial statements have been approved for issue by the Council and the Board of Directors on 21 March 2014.

NOTE 2 OPERATING ENVIRONMENT OF THE BANK

Instability in the global and Latvian financial markets and economies
Although Latvia is now often mentioned as a success story and model for overcoming the economic crisis, it should be noted that there are significant risks to the success of economic growth in the future. It is based on the stagnation in the European Union and the Russian economic slowdown, the negative scenario development may significantly slow down the export of a post-crisis period, the country's economic growth and cost reductions enabled the successful development of the industrial sector. Although the macro-economic trends in the internal market and the Latvian trade partner markets show a relatively low probability of occurrence of such a scenario, both the public sector and the private sector maintain moderate optimism and guard against the negative global economic scenarios.

After joining the Eurozone, Latvia transferred control of interest rates in the hands of the European Central Bank and in accordance with the latest analysts' forecasts euro base rate close to zero is likely to remain for all 2014 and most of 2015. Therefore, it is unlikely to occur with commercial banks deposit with the increase in costs in the near future. In turn, interest rates on loans are not on their historically low levels and banks have the potential to stimulate lending to customers by lowering interest rates and credit availability requirements.

Impact on borrowers
Borrowers of the Bank may be affected by the lower liquidity situation which could in turn impact their ability to repay the amounts owed. Deteriorating operating conditions for borrowers may also have an impact on management's cash flow forecasts and assessment of the impairment of financial and non-financial assets. To the extent that information is available, management has properly reflected revised estimates of expected future cash flows in its impairment assessments.

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

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARIES OF SIGNIFICANT ACCOUNTING POLICIES

A summary of the significant accounting policies, all of which have been applied consistently throughout the years 2012 and 2013, are set out below:

(a) Reporting currency

The tabular amounts in the accompanying financial statements are reported in Latvian lats (LVL), unless otherwise stated.

(b) Basis of preparation

These financial statements are prepared in accordance with International Financial Reporting Standards as adopted in 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 Bank's financial position, access to financial resources and analysed the impact of the recent financial crisis on the future operations of the Bank.

The financial statements are prepared under the historical cost convention as modified by the fair valuation of financial assets held at fair value through profit or loss and derivative financial instruments.

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 Management's best knowledge of current events and actions, actual results ultimately may differ from those estimates.

The accounting policies used in the preparation of the financial statements for the year ended 31 December 2013 are consistent with those used in the annual financial statements for the year ended 31 December 2012, except as referred to in Note 3 (bb) *Adoption of New or Revised Standards and Interpretations*.

(c) Income and expense recognition

Interest income and expense are recognised in the statement of comprehensive income for all interest bearing instruments on an accrual basis using the effective interest method. Interest income includes coupons earned on trading securities.

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability.

When loans become doubtful of collection, they are written down to their recoverable amounts and interest income is thereafter recognised based on the rate of interest that was used to discount the future cash flows for the purpose of measuring the recoverable amount.

Commissions received or incurred in respect of origination of financial assets or funding are deferred and recognised as an adjustment to the effective interest rate on the asset or liability. Other fees and commissions, including those related to trust activities, are credited and/or charged to the statement of comprehensive income as earned / incurred.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(d) Foreign currency translation

Functional and presentation currency
Items included in the financial statements of the Bank are measured using the currency of the primary economic environment in which the entity operates (‘the functional currency’). The financial statements are presented in ‘Latvian lats’ (‘LVL’), which is the Bank’s functional and presentation currency.

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

The principal rates of exchange (LVL to 1 foreign currency unit) set forth by the Bank of Latvia and used in the preparation of the Bank’s balance sheets were as follows:

Reporting date	USD	EUR	UAH
As at 31 December 2013	0.515	0.702804	0.0623
As at 31 December 2012	0. 531	0.702804	0.0660

(e) Income taxes

Income tax is calculated in accordance with Latvian tax regulations and is based on the taxable income reported for the taxation period.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. The deferred income tax is calculated based on currently enacted tax rates that are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

The principal temporary differences arise from different rates of accounting and tax amortisation and depreciation on intangible and fixed assets, as well as accruals for employee vacation expenses. Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

(f) 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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(g) Loans and provisions for loan impairment

Loans and advances to customers are accounted for as loans and receivables. Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in active markets.

Loans and receivables are recognised initially at fair value plus transaction costs that are directly attributable to the acquisition of financial asset. Loans and receivables are subsequently carried at amortised cost using the effective interest method. All loans and receivables are recognised when cash is advanced to borrowers and derecognised on repayments.

The Bank assesses at each balance sheet date whether there is objective evidence that loans and receivables are impaired. If any such evidence exists, the amount of the loss for loan impairment which has been incurred is measured as the difference between the asset's carrying amount and the recoverable amount, being the present value of expected cash flows (excluding future credit losses that have not been incurred), including amounts recoverable from guarantees and collateral, discounted at the original effective interest rate. The Bank does not perform collective assessment of provisions as it can carry out assessment of each individual loan taken the number of loans issued.

The primary factors that the Bank considers in determining whether a financial asset is impaired are its overdue status and realisability of related collateral, if any.

The following other principal criteria are also used to determine whether there is objective evidence that an impairment loss has occurred:

- any instalment is overdue and the late payment cannot be attributed to a delay caused by the settlement systems;
- the borrower experiences a significant financial difficulty as evidenced by the borrower's financial information that the Bank obtains;
- the borrower considers bankruptcy or a financial reorganisation;
- there is an adverse change in the payment status of the borrower as a result of changes in the national or local economic conditions that impact the borrower; or
- the value of collateral significantly decreases as a result of deteriorating market conditions.

The carrying amount of the asset is reduced through the use of a provision account and the amount of the loss is recognised in the statement of comprehensive income. The assessment of the evidence for impairment and the determination of the amount of provision for impairment or its reversal require the application of Management's judgment and estimates. Management's judgments and estimates consider relevant factors including, but not limited to, the identification of non-performing loans and high risk loans, the Bank's past loan loss experience, known and inherent risks in the portfolio of loans, adverse situations that affects the borrowers' ability to repay, the estimated value of any underlying collateral and current economic conditions as well as other relevant factors affecting loan and advance recoverability and collateral values. These judgments and estimates are reviewed periodically, and historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. The Management of the Bank has made their best estimates of losses, based on objective evidence of impairment and believes those estimates presented in the financial statements are reasonable in light of available information. Nevertheless, it is reasonably possible, based on existing knowledge, that outcomes within the next financial year that are different from assumptions could require a material adjustment to the carrying amount of the asset or liability affected.

When loans and receivables cannot be recovered, they are written off and charged against provision for loan impairment losses. They are not written off until all the necessary legal procedures have been completed and the amount of the loss is finally determined.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(h) Credit related commitments

The Bank enters into credit related commitments, including undrawn credit lines, letters of credit and financial guarantees. Financial guarantees represent irrevocable assurances to make payments in the event that a customer cannot meet its obligations to third parties and carry the same credit risk as loans. Financial guarantees and commitments to provide a loan are initially recognised at their fair value, which is normally evidenced by the amount of fees received. This amount is amortised on a straight line basis over the life of commitment, except for commitments to originate loans if it is probable that the Bank will enter into a specific lending arrangement and does not expect to sell the resulting loan shortly after the origination; such loan commitment fees are deferred and included in the carrying value of the loan on initial recognition. At each balance sheet date, the commitments are measured at the higher of (i) the remaining unamortised balance of the amount at initial recognition and (ii) the best estimate of expenditure required settling the commitment at the balance sheet date.

(i) 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 at inception. Financial assets at fair value through profit or loss comprise debt securities held by 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 recognised at trade date, which is the date that the Bank commits to purchase or sell the asset.

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

(j) Sale and repurchase agreements of securities

Sale and repurchase agreements are accounted for as financing transactions. Under sale and repurchase agreements, where the Bank is a transferor, assets transferred remain on the Bank’s balance sheets and are subject to the 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 Bank’s balance sheet, 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 recognised in the statement of comprehensive income over the term of the agreement using the effective interest method.

(k) Derivative financial instruments

Derivative financial instruments include foreign exchange contracts, currency and interest rate swaps held by the Bank for trading purposes. Derivative financial instruments are recognised on trade date and categorised as financial assets at fair value through profit or loss. They are initially recognised in the balance sheet at fair value and subsequently measured at their fair value with all gains and losses from revaluation reported in the statement of comprehensive income. All derivatives are carried as financial assets when fair value is positive and as financial liabilities when fair value is negative.

(l) Due from other banks

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

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(m) 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 price 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. Fair values of financial assets or liabilities, including derivative financial instruments, in active markets are based on quoted market prices. If the market for a financial asset or liability is not active (and for unlisted securities), the Bank establishes fair value by using valuation techniques. These include the use of discounted cash flow analysis, option pricing models and recent comparative transactions as appropriate, and may require the application of management's judgment and estimates.

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

(n) Derecognition of financial assets

The Bank derecognises financial assets when (i) the assets are redeemed or the rights to cash flows from the assets otherwise expired or (ii) the Bank has transferred substantially all the risks and rewards of ownership of the assets or (iii) the Bank has neither transferred nor retained substantially all risks and rewards of ownership but has not retained control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose additional restrictions on the sale.

(o) Intangible assets

Acquired computer software licences are recognised as intangible assets on the basis of the costs incurred to acquire and bring to use the software. These costs are amortised on the basis of their expected useful lives, not exceeding five years.

(p) Property and Equipment

All property and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. 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 using the straight-line method to allocate cost of the fixed assets to their residual values over their estimated useful lives, as follows:

Office equipment	10 years
Computers	3 years
Transport	5 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

Leasehold improvements are capitalised and depreciated over their expected useful lives, or over the remaining lease contract period if shorter, on a straight-line basis.

Property and equipment are periodically reviewed for impairment. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use.

Gains or losses on disposals are determined by comparing carrying amount with proceeds and are charged to the statement of comprehensive income in the period in which they are incurred.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(q) Operating lease – the Bank is a lessee

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any financial incentives received from the lessor) are charged to the statement of comprehensive income on a straight-line basis over the period of the lease.

(r) Customer accounts

Customer accounts are non-derivative liabilities to individuals, state or corporate customers and are carried at amortised cost.

(s) Borrowings

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

(t) Provisions

Provisions are recognised when the Bank has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made. The assessment of provisions requires the application of management's judgment and estimates, as to the probability of an outflow of resources, the probability of recovery of resources from corresponding sources including security or collateral or insurance arrangements where appropriate, and the amounts and timings of such outflows and recoveries, if any.

(u) Dividends

Dividends are recorded in equity in the period in which they are declared. Dividends declared after the balance sheet date and before the financial statements are authorised for issue are disclosed in the subsequent events note. The statutory accounting reports of the Bank are the basis for profit distribution and other appropriations. Latvian legislation identifies the basis of distribution as retained earnings.

(v) Employee benefits

The Bank pays State compulsory social security contributions for state pension insurance and to the state funded pension scheme in accordance with Latvian legislation. State funded pension scheme is a defined contribution plan under which the Bank pays 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 state funded pension scheme are not able to settle their liabilities to employees. According to the rulings of the Cabinet of Ministers of the Republic of Latvia 75,80% (2012: 76.20%) of the social security contributions are used to finance state funded pension scheme.

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

(w) Off-balance sheet instruments

In the ordinary course of business, the Bank utilises off-balance sheet financial instruments including commitments to extend loans and advances, financial guarantees and commercial letters of credit. Such financial instruments are recorded in the financial statements when they are funded or related fees are incurred or received. The methodology for provisioning against off-balance sheet instruments is given in paragraph (t) of Note 3 above.

(x) Trust operations

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

Accounting for trust operations is separated from the 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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(y) Debt securities in issue

Debt securities in issue include bonds issued by the Bank. Debt securities are stated at amortised cost. If the Bank purchases its own debt securities in issue, they are removed from the balance sheet and the difference between the carrying amount of the liability and the consideration paid is included in gains arising from retirement of debt.

(z) Offsetting of Financial Assets and Liabilities

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

(aa) Critical accounting estimates

Loan impairment

The Bank reviews its loan portfolio to assess impairment on a regular basis. In determining whether an impairment loss should be recorded in the statement of comprehensive income, the Bank's Management makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio.

This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

The Bank applies stress – tests in order to evaluate the impact of changes in one or a number of variables, which are used for determination of provisions for loan impairment losses, on the financial result. If overdue loans in loan portfolio increase by 1%, provisions for loan impairment losses would increase by LVL 141.2 thousand.

Securities valued at fair value.

The Bank used quoted market prices to value securities carried at fair value as at year end for those securities which in the management's judgement are traded at liquid markets. The management had evaluated the liquidity of the securities market and has concluded that there is a significant reduction of activities in market, however, consider the market to be active with respect to type of securities held by the Bank therefore quoted market prices available on Stock Exchange of the security issuer countries were used to determine the fair values of the securities as at year end.

Initial recognition of related party transactions

In the normal course of business the Bank enters into transactions with its related parties. IAS 39 requires initial recognition of financial instruments based on their fair values. Management's judgement is applied in determining if transactions are priced at market or non-market interest rates, where there is no active market for such transactions. The basis for judgement is pricing for similar types of transactions with unrelated parties and effective interest rate analysis.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(bb) Adoption of new or revised standards and interpretations

The following new and amended IFRSs and interpretations became effective in 2013 (as adopted by the European Union (EU)):

IFRS 13, ‘Fair value measurement’ (effective for annual periods beginning on or after 1 January 2013) improved consistency and reduced complexity by providing a revised definition of fair value, and a single source of fair value measurement and disclosure requirements for use across IFRSs.

The following new and amended IFRS and interpretations became effective in 2013, but have no significant impact on these financial statements:

Annual improvements 2011 (effective for annual periods beginning on or after 1 January 2013);

Amendment to IFRS 1, ‘First time adoption’, on government loans (effective for annual periods beginning on or after 1 January 2013);

Amendment to IFRS 7, ‘Financial instruments: Disclosures’, on offsetting financial assets and financial liabilities (effective for annual periods beginning on or after 1 January 2013);

Amendment to IAS 12, ‘Income taxes’ on deferred tax (effective for annual periods beginning on or after 1 January 2012 but endorsed by EU for annual periods beginning on or after 1 January 2013);

Amendment to IAS 19, ‘Employee benefits’ (effective for annual periods beginning on or after 1 January 2013);

IFRIC 20, ‘Stripping costs in the production phase of a surface mine’ (effective for annual periods beginning on or after 1 January 2013);

Amendment to IAS 1 „Presentation of Financial Statements” (effective for annual periods beginning on or after 1 July 2013).

A number of new standards and interpretations have been published and becomes effective for annual periods beginning on or after 1 January 2014, or which are not yet approved in the European Union.

IFRS 10, ‘Consolidated financial statements’ (effective for annual periods beginning on or after 1 January 2013, endorsed by EU for annual periods beginning on or after 1 January 2014);

IFRS 11, ‘Joint arrangements’ (effective for annual periods beginning on or after 1 January 2013 although endorsed by EU for annual periods beginning on or after 1 January 2014);

IFRS 12, ‘Disclosures of interests in other entities’ (effective for annual periods beginning on or after 1 January 2013 although endorsed by EU for annual periods beginning on or after 1 January 2014);

Amendments to IFRS 10, 11 and 12 on transition guidance (mandatory application for annual periods beginning on or after 1 January 2014 with early adoption allowed, endorsed by EU for annual periods beginning on or after 1 January 2014);

IFRS 14 “Regulatory Deferral Account” (effective for annual periods beginning on ot after 1 January 2016, not yet endorsed by the EU)

IAS 27 (revised in 2011) ‘Separate financial statements’ (effective for annual periods beginning on or after 1 January 2013 although endorsed by EU for annual periods beginning on or after 1 January 2014);

IAS 28 (revised in 2011) ‘Associates and joint ventures’ (effective for annual periods beginning on or after 1 January 2013 although endorsed by EU for annual periods beginning on or after 1 January 2014);

Amendments to IAS 19 “Employee benefits plans” (effective for annual periods beginning on or after 1 January 2014, not yet endorsed by the EU);

Amendments to IAS 32 “Financial instruments: Presentation”, on offsetting financial assets and financial liabilities (effective for annual periods beginning on or after 1 January 2014, not yet endorsed by the EU);

Amendments to IFRS 10, IFRS 12 and IAS 27 for investment entities (effective for annual periods beginning on or after 1 January 2014, not yet endorsed by the EU);

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(bb) Adoption of new or revised standards and interpretations (continued)

IFRS 9 "Financial Instruments - Classification and Measurement" (effective date to be determined, not yet endorsed by the EU);

Amendments to IAS 36 "Impairment of assets" (effective for annual periods beginning on or after 1 January 2014);

Amendments to IAS 39 "Financial instruments: Recognition and measurement', on novation of derivatives and hedge accounting (effective for annual periods beginning on or after 1 January 2014);

Annual improvements 2012 (effective for annual periods beginning on or after 1 July 2014, not yet endorsed by the EU);

Annual improvements 2013 (effective for annual periods beginning on or after 1 July 2014, not yet endorsed by the EU);

IFRIC 21 'Levies' (effective for annual periods beginning on or after 1 January 2014, not yet endorsed by the EU).

NOTE 4 FINANCIAL RISK MANAGEMENT

Risk Management

Risk management is one of the Bank's strategic tasks. Risk management strategy has been developed for the Bank's risk management, which covers management of the following risks: credit risk and residual risk, operational risk, market risk, interest rate risk, foreign currency risk, liquidity risk, concentration risk, country 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 Bank's Council and/or Board and implemented by the responsible units of the Bank.

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

The main unit responsible for determination, evaluation and oversight of the 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 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 Bank in accordance with the provisions of the contract. Credit risk is present in the Bank's operations where the Bank makes claims against another person and which are reflected in the Bank's balance sheet and 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 Bank divides up and oversees its credit risk by setting limits of various types and categories: acceptable risk limits for each borrower, group of related borrowers, geographical regions, business sectors, type and value of collateral, currency, term and ratings granted by international agencies. Credit risk exposures are monitored on a revolving basis through regular assessments of borrowers' ability to meet interest and principal repayments and limits are adjusted as appropriate. The Bank's exposure to credit risk is managed and minimised by obtaining collaterals and guarantees against credit exposures that are registered in the name of the Bank. The fair values of those are also reviewed on a regular basis.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 4 FINANCIAL RISK MANAGEMENT (continued)

(a) Credit risk (continued)

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

	31.12.2013 LVL	31.12.2012 LVL
Credit risk exposures relating to on-balance sheet assets are as follows:		
Due from credit institutions	222,195,264	207,381,802
Loans to customers	49,090,287	72,830,308
Financial assets at fair value through profit or loss	16,555,553	13,793,922
Other assets	3,145,387	1,477,816
Total	**290,986,491**	**295,483,848**
Credit risk exposures relating to off-balance sheet items are as follows:		
Contingent liabilities	2,399,357	6,016,694
Financial commitments	26,030,282	19,170,535
Total	**28,429,639**	**25,187,229**

(b) Market risk

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

The Bank manages market risks by diversification of financial instruments portfolio, limits set for different types of financial instruments and application of sensitivity tests which show the impact of particular risks on the Bank’s assets and equity.

(c) Currency risk

The Bank has exposure to the effects of fluctuations in prevailing foreign currency exchange rates as a result of its financial position and cash flows. The Bank seeks to match assets and liabilities denominated in foreign currencies in order to avoid foreign currency exposures. The Board has set limits on the level of exposure by currency, which is monitored on a daily basis. The Latvian banking legislation requires that open positions in each foreign currency may not exceed 10% of the Bank’s equity and that the total foreign currency open position may not exceed 20% of the equity. During 2013 the Bank was in compliance with those limits (see Note 25).

The Bank’s foreign currency risk evaluation is based on the following main principles:
- evaluation is made of changes to the Bank’s assets, liabilities and off-balance sheet items as a result of exchange rate fluctuations;
- how the Bank’s revenue/costs change with exchange rate fluctuations;
- performance of currency risk stress tests.

The main elements of currency risk management:
- currency risk evaluation;
- setting of limits and restrictions;
- monitoring of adherence to internal limits;
- performance of exchange rate stress tests and analysis of obtained results;
- entering into hedging relationships if necessary.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 4 FINANCIAL RISK MANAGEMENT (continued)

(c) Currency risk (continued)

Sensitivity Analysis

The following table shows the sensitivity of profit/loss and equity to currency exchange rate fluctuations at the end of the reporting period, with other conditions constant:

31.12.2013	**Effect on equity**		**Effect on profit/loss**		**31.12.2012**	**Effect on equity**		**Effect on profit/loss**	
	+100 bps	**-100 bps**	**+100 bps**	**-100 bps**		**+100 bps**	**-100 bps**	**+100 bps**	**-100 bps**
USD	-320	320	41	-41	**USD**	233	233	-12	12
EUR	-127	127	2	-2	**EUR**	-9	9	16	-16
LVL	234	-234	1	-1	**LVL**	201	-201	1	-1
Other	-	-	-	-	**Other**	-	-	-	-
Total	**-213**	**213**	**44**	**-44**	**Total**	**-41**	**41**	**5**	**-5**

The following table shows the average annual sensitivity of profit/loss and equity to currency exchange rate fluctuations during the reporting period, with other conditions constant:

31.12.2013	**Effect on equity**		**Effect on profit/loss**		**31.12.2012**	**Effect on equity**		**Effect on profit/loss**	
	+100 bps	**-100 bps**	**+100 bps**	**-100 bps**		**+100 bps**	**-100 bps**	**+100 bps**	**-100 bps**
Total	**2**	**-2**	**-7**	**7**	**Total**	**-164**	**164**	**17**	**-17**

(d) Interest rate risk

Interest rate risk is the sensitivity of the financial position of the Bank to a change in market interest rates. In the normal course of business, the Bank encounters 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 Bank (see Note 27).

In order to evaluate interest rate risk, evaluation is made of the impact of interest rate changes on the Bank's economic value, including evaluation of interest rate risk from the revenue perspective and the economic value perspective. In addition, interest rate risk stress testing is performed.

The main elements of interest rate risk management:
- evaluation of interest rate risk sensitivity;
- setting of internal limits (limit of reduction in economic value and for total duration of securities portfolio);
- monitoring of adherence to internal limits;
- performance of interest rate stress tests and analysis of obtained results;
- entering into hedging relationships if necessary.

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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 4 FINANCIAL RISK MANAGEMENT (continued)

(d) Interest rate risk (continued)

The following table shows the sensitivity of profit/loss and equity to interest rate fluctuations with other conditions constant:

31.12.2013	Effect on equity		Effect on profit/loss		31.12.2012	Effect on equity		Effect on profit/loss	
	+100 bps	-100 bps	+100 bps	-100 bps		+100 bps	-100 bps	+100 bps	-100 bps
USD	-172	172	1 619	-1 619	**USD**	-141	141	1 404	- 1 404
EUR	-38	38	329	-329	**EUR**	-133	133	21	-21
LVL	-220	220	-14	14	**LVL**	-166	166	93	-93
Other	-	-	34	-34	**Other**	-	-	24	-24
Total	**-430**	**430**	**1 968**	**- 1 968**	**Total**	**-441**	**441**	**1 542**	**-1 542**

The following table shows the average annual sensitivity of profit/loss and equity to interest rate fluctuations, with other conditions constant:

31.12.2013	Effect on equity		Effect on profit/loss		31.12.2012	Effect on equity		Effect on profit/loss	
	+100 bps	-100 bps	+100 bps	-100 bps		+100 bps	-100 bps	+100 bps	-100 bps
Total	**-448**	**448**	**1 805**	**-1 805**	**Total**	**-403**	**403**	**1 460**	**-1 460**

(e) Liquidity risk

The Bank is 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 Bank does 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. The Board sets limits on the minimum proportion of maturing funds available to meet such calls and on 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 26). 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 Bank and its exposure to changes in interest rates and exchange rates.

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

The Bank uses 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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 4 FINANCIAL RISK MANAGEMENT (continued)

(e) Liquidity risk (continued)
The following are the main elements of liquidity risk management:
- being in compliance with liquidity ratio regulations;
- setting of the liquidity net position limit;
- setting of restriction for attracting deposits;
- monitoring of adherence to liquidity limits;
- conducting liquidity stress tests and analysis of results obtained;
- recommendations for resolving liquidity problems.

In accordance with 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 Bank's capital resources to cover risks resulting from the 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:
-the capital requirements for the credit risk are calculated using the standardised approach,
-"simple method of financial security" is used in order to decrease the credit risk,
-the capital requirements for the foreign exchange risks, capital requirements for the commodities risk, capital requirements for the position risk of debt securities and equities are calculated using the standardised approach,
-the capital requirements for the general risk of debt securities are calculated using maturity method;
-the capital requirements for the operational risk are calculated using the basic index approach.

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

Moreover, the Bank has developed internal documentation and regulations according to which it determines 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).

Calculated in accordance with the FCMC requirements, the Bank's capital adequacy ratio as at 31 December 2013 was 21.64% (as at 31 December 2012 22.13%), which is above the minimum required by the FCMC since year 2007. FCMC requires Latvian banks to maintain a capital adequacy ratio of 8% of weighted assets and off-balance sheet items which are calculated in accordance with the rules set by FCMC (see also Note 24). According to the requirements of FCMC individual capital requirement was set for the Bank in September 2013 at 13.9% which the Bank observes and complies with.

(g) Operational risk
Operational risk is the possibility of incurring losses as a result of inadequate or unsuccessful developments in the 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 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 Bank has established and maintains an Operational Risk Event and Loss database in which internal data on operational risk events and associated losses are collected, processed and organised.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 4 FINANCIAL RISK MANAGEMENT (continued)

(g) Operational risk (continued)

The main elements of operational risk management are:

- operational risk monitoring;
- operational risk control and minimisation:
  - development of internal regulatory documents which prevent/reduce the likelihood of operational events;
  - segregation of duties;
  - control over internal limits;
  - adherence to the procedures in the use of IT and other Bank’s resources;
  - appropriate training of employees;
  - regular review of supporting documents for transactions and account balances.

(h) Concentration risk

Transaction concentration risk is each and every risk deal or group of risk deals that could cause Bank to suffer such losses that may endanger the liquidity of the Bank or its ability to continue on a going concern. Concentration risk arises from significant risk deals with Clients or Group of inter-related Clients or risk deals with Clients with common risk factors (e.g., economy sector, geographical region, currency, instrument used for decrease of credit risk (one type of collateral or one provider of collateral, etc.).

In order to control transaction concentration risk Bank has set limits for 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.

Country risk is one of significant transaction concentration risks. Country risk – country partner risk – is the possibility of incurring losses if the Bank’s assets are located in a country where, due to changes in its economic and political factors, 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, unfavourable legislative changes, creation of new restrictions and barriers as well as other, including force majeure, factors.

In order to control concentration risks following limits were set:

- currency 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 high risk deals;
- limits on transactions with parent bank;
- limits on crediting programmes.

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

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

The main elements of risk control:

- setting of internal limits for 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 client 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 state risk is transferred to the country where the loan collateral is actually located.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 5 INTEREST INCOME AND EXPENSE

	2013 LVL	2012 LVL
Interest income		
Loans and advances to legal entities	3,973,269	5,544,157
Loans and advances to private individuals	196,488	220,373
Balances due from banks	8,291,178	7,867,724
Trading securities	753,803	559,220
Total interest income	**13,214,738**	**14,191,474**
Interest expense		
Due to private individuals	(768,252)	(1,009,416)
Due to legal entities	(3,986,230)	(6,369,898)
Subordinated loan	(495,079)	(472,652)
Other liabilities	(651,504)	(941,576)
Total interest expense	**(5,901,065)**	**(8,793,542)**
Net interest income	**7,313,673**	**5,397,932**

NOTE 6 FEE AND COMMISSION INCOME AND EXPENSE

	2013 LVL	2012 LVL
Fee and commission income		
Money transfers	3,335,428	2,758,535
Loan related fees	1,860	611
Accounts servicing	27,253	-
Letters of credit	404,389	315,908
Sale of deposit certificates	372,583	320,928
Commission income on transactions with financial instruments	41,014	34,034
Commission income on current accounts	26,869	15,563
Income from general services	61,143	56,024
Other commissions (DIGIPAS)	30,011	23,737
Interbank commission income	92,791	73,759
Commission for dealing with cards	116,360	104,242
Income from currency exchange	140,232	179,678
Other income	133,214	114,766
Total fee and commission income	**4,783,147**	**3,997,785**
Fee and commission expense		
Money transfers	(1,076,682)	(1,178,500)
Other expense	(20,904)	(49,964)
Total fee and commission expense	**1,097,586**	**(1,228,464)**
Net fee and commission income	**3,685,561**	**2,769,321**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 7 ADMINISTRATIVE EXPENSE

	2013 LVL	2012 LVL
Remuneration paid to personnel	1,777,134	1,790,469
Rent expense	283,931	306,226
Office and equipment maintenance	73,926	75,590
Remuneration paid to the members of the Council and the Board	213,281	221,373
Security services	1,935	15,292
Public utilities	36,897	36,703
State compulsory social insurance contributions	479,559	469,935
Communication expense	222,777	214,919
Consulting and professional fees	424,747	463,115
Set-up and maintenance costs of information systems	77,061	77,250
Business trips	76,602	76,730
Credit card expenses	20,631	-
Transportation	37,297	41,563
Health insurance	19,875	18,765
Advertising and marketing	4,378	2,010
Penalties	-	208
Other administrative expense	471,844	394,177
	4,221,875	**4,204,325**

The average number of staff employed by the Bank in 2013 was 130 (2012: 127).

NOTE 8 INCOME TAX EXPENSE

Corporate income tax for the reporting year	-	-
Amount of tax paid abroad	858,814	816,577
Change in deferred tax (see Note 19)	(20,521)	13,577
Total corporate income tax	**838,293**	**830,154**

Corporate income tax differs from the theoretically calculated taxation at the 15% rate as stipulated by the law (see below):

Profit before income tax	**1,503,007**	**2,370,002**
Theoretically calculated tax at a tax rate of 15%	225,451	355,500
Loss from revaluation of securities at fair value through profit and loss account, net	(30,219)	(97,750)
Other expenses not deductible for tax purposes, net	(215,753)	(244,173)
Amount of tax paid abroad	858,814	816,577
Corporate income tax expense	**838,293**	**830,154**

Deferred income tax is calculated by using the enacted tax rate – 15%.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 9 CASH AND BALANCES WITH THE BANK OF LATVIA

	31.12.2013 LVL	31.12.2012 LVL
Cash	796,892	687,627
Balances on demand with the Bank of Latvia	22,291,374	43,753,230
	23,088,266	**44,440,857**

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

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 monetary means in the account can be freely accessed and used by the Bank. The minimum level of the Bank's correspondent account for the period from 24 December 2013 to 31 December 2013 was set at LVL 11,519,940.

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

NOTE 10 BALANCES DUE FROM BANKS

	31.12.2013 LVL	31.12.2012 LVL
Due from Republic of Latvia credit institutions	26,775,482	8,490,321
Due from non-OECD credit institutions	101,307,192	145,223,130
Due from OECD credit institutions	94,112,590	53,668,351
	222,195,264	**207,381,802**

The following table discloses balances due from banks based on their type:

On demand	98,331,654	180,118,610
Balances with maturity of three months or less	71,260,394	4,168,839
Other balances due from banks	52,603,216	23,094,353
	222,195,264	**207,381,802**

The following table discloses balances due from banks according to their ratings as at 31 December 2013 and 31 December 2012:

	31.12.2013		**31.12.2012**	
Rating	**Due from banks LVL**	**%**	**Due from banks LVL**	**%**
From Aaa to Aa3	244,498	0,11%	58	0,00%
From A1 to A3	84,954,076	38,23%	52,523,410	25,33%
From Baa1 to Baa3	22,849,278	10,28%	5,508,003	2,65%
From Ba1 to Ba3	11,112,315	5,00%	475,230	0,23%
From B1 to B3	12,154,834	5,47%	11,327,240	5,46%
Below B3	46,515,679	20,93%	114,911,275	55,41%
Total	**177,830,680**	**80,02%**	**184,745,216**	**89,08%**
Without rating	44,364,584	19,98%	22,636,586	10,92%
	222,195,264	**100,00%**	**207,381,802**	**100,00%**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 11 LOANS AND ADVANCES TO CUSTOMERS

Analysis of loans by client type and by products

	31.12.2013 LVL	31.12.2012 LVL
Loans to legal entities:		
Loans to private individuals, except for mortgages	60,143,422	77,091,807
Loans to private individuals – private enterprises	1,226,850	1,490,031
Mortgages	1,565,839	2,268,765
Sale and repurchase agreements (reverse repo)	-	2,291,143
Less: provisions for loan impairment	(13,845,824)	(10,311,438)
Total loans and advances to customers	**49,090,287**	**72,830,308**

The following table discloses changes in provisions for loan impairment during 2013:

	Loans to legal entities	Loans to private individuals, except for mortgages	Mortgages	Total
Provisions for loan impairment as at 1 January 2013	**9,549,584**	**553,249**	**208,605**	**10,311,438**
Increase in provisions for loan impairment for the year	5,072,210	592,354	215,867	5,880,431
Change in provision due to loans write-offs	(2,007,714)	-	-	(2,007,714)
Impact of foreign currency revaluation	(338,331)	-	-	(338,331)
Provisions for loan impairment as at 31 December 2013	**12,275,749**	**1,145,603**	**424,472**	**13,845,824**

The following table discloses changes in provisions for loan impairment during 2012:

	Loans to legal entities	Loans to private individuals, except for mortgages	Mortgages	Total
Provisions for loan impairment as at 1 January 2012	**8,600,593**	**330,762**	**350,435**	**9,281,790**
Increase in provisions for loan impairment for the year	2,970,282	229,907	-	3,200,189
Change in provision due to loans write-offs	(1,915,473)	-	(149,264)	(2,064,737)
Impact of foreign currency revaluation	(105,818)	(7,420)	7,434	(105,804)
Provisions for loan impairment as at 31 December 2012	**9,549,584**	**553,249**	**208,605**	**10,311,438**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 11 LOANS AND ADVANCES TO CUSTOMERS (continued)

The concentration of risks in the credit portfolio based on the economical industries is as follows:

	2013		2012	
	LVL	**%**	**LVL**	**%**
Trade and commercial activities	20,363,630	32.36	32,249,466	38,79
Private individuals	2,792,689	4.44	3,758,796	4,52
Agriculture and food industry	3,215,040	5.11	5,011,642	6,03
Construction and operations with real estate	15,349,918	24.39	16,569,359	19,93
Transport and communication	9,114,011	14.48	11,808,650	14,20
Industry	4,332,313	6.88	3,953,200	4,75
Tourism and hotel services, restaurant business	938,683	1.49	1,912,167	2,30
Financial services	3,147,361	5.00	4,240,886	5,10
Other	3,682,466	5.85	3,637,580	4,38
Loans and advances to customers (before provisions for impairment)	**62,936,111**	**100.00**	**83,141,746**	**100.00**

As at 31 December 2013, the total amount of loans issued to 10 largest customers was LVL 26,511,145 (2012: LVL 29,283,581), which comprises 42.12% of the total credit portfolio (2012: 35.22%). As at 31 December 2013, there were loans and advances to customers secured by deposits LVL 5,215,845.

The following table shows the information about collateral as at 31 December 2013:

	Loans to legal entities	**Loans to private individuals, except for mortgages**	**Loans to private individuals – private enterprises**	**Mortgages**	**Total**
Unsecured	5,027,940	1,221,323	-	208,385	6,457,648
Collateralised by:					
- residential real estate	1,445,792	-	-	724,853	2,170,645
- other real estate	31,555,126	-	-	632,601	32,187,727
- tradable securities	-	-	-	-	-
- cash deposits	6,437,324	5,527	-	-	6,442,851
- other assets	15,677,240	-	-	-	15,677,240
Total loans and advances to customers (before provisions for impairment)	**60,143,422**	**1,226,850**	**-**	**1,565,839**	**62,936,111**

The following table shows the information about collateral as at 31 December 2012:

	Loans to legal entities	**Loans to private individuals, except for mortgages**	**Loans to private individuals – private enterprises**	**Mortgages**	**Total**
Unsecured	3,547,089	168,089	-	209,587	3,924,765
Collateralised by:					
- residential real estate	3,521,115	-	-	827,043	4,348,158
- other real estate	44,010,931	1,321,793	-	1,232,135	46,564,859
- tradable securities	3,345,478	-	-	-	3,345,478
- cash deposits	6,480,920	149	-	-	6,481,069
- other assets	18,477,417	-	-	-	18,477,417
Total loans and advances to customers (before provisions for impairment)	**79,382,950**	**1,490,031**	**-**	**2,268,765**	**83,141,746**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 11 LOANS AND ADVANCES TO CUSTOMERS (continued)

The following table shows the loans outstanding as at 31 December 2013 by credit quality:

	Loans to legal entities	**Loans to private individuals, except for mortgages**	**Loans to private individuals – private enterprises**	**Mortgages**	**Total**
Loans that are neither past due nor impaired					
- Standard loans	31,644,408	75,842	-	609,497	**32,329,747**
- Close control	203,624	-	-	-	**203,624**
- Under the standard credit	-	-	-	-	**-**
Total neither past due nor impaired	**31,848,032**	**75,842**	**-**	**609,497**	**32,533,371**
Past due but not impaired					
- past due 30 days	3,009,285	-	-	-	**3,009,285**
- past due from 30 to 90 days	1,857,326	-	-	-	**1,857,326**
- past due from 91 to 180 days	1,522,474	-	-	-	**1,522,474**
Total past due, but not impaired	**6,389,085**	**-**	**-**	**-**	**6,389,085**
Individually impaired loans ***(total amount)***					
- not past due	9,855,473	7,418	-	-	**9,862,891**
- past due up to 30 days	-	13,580	-	-	**13,580**
- past due 30 – 90 days				719,557	**719,557**
- past due 91 – 180 days	799,088	-	-	-	**799,088**
- past due 181 – 360 days	1,723,392	454	-	-	**1,723,846**
- past due over 360 days	9,528,352	1,129,556	-	236,785	**10,894,693**
Total individually impaired loans (total amount)	**21,906,305**	**1,151,008**	**-**	**956,342**	**24,013,655**
Less: provisions for loan impairment	**(12,275,749)**	**(1,145,603)**	**-**	**(424,472)**	**(13,845,824)**
Net loans and advances to customers	**47,867,673**	**81,247**	**-**	**1,141,367**	**49,090,287**

Loans past due, but not impaired include all amounts due from borrowers. Amount actually overdue as at 31 December 2013 was 4,180,116 LVL.

Loans past due and individually impaired include all amounts due from borrowers. Amount actually overdue as at 31 December 2013 was 12,005,641 LVL.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 11 LOANS AND ADVANCES TO CUSTOMERS (continued)

The following table shows the loans outstanding as at 31 December 2012 by credit quality:

	Loans to legal entities	**Loans to private individuals, except for mortgages**	**Loans to private individuals – private enterprises**	**Mortgages**	**Total**
Loans that are neither past due nor impaired					
- Standard loans	55,345,447	136,907	-	828,351	**56,310,705**
- Close control	203,670	-	-	-	**203,670**
- Under the standard credit	-	-	-	-	**-**
Total neither past due nor impaired	**55,549,116**	**136,907**	**-**	**828,351**	**56,514,374**
Past due but not impaired					
- past due 30 days	53,391	-	-	-	**53,391**
- past due from 30 to 90 days	5,510,074	-	-	-	**5,510,074**
- past due from 91 to 180 days	523,526	2,796	-	-	**526,322**
- past due 181 – 360 days	62,367	-	-	308,532	**370,899**
- past due over 360 days	-	-	-	895,203	**895,203**
Total individually impaired loans (total amount)	**6,149,358**	**2,796**	**-**	**1,203,735**	**7,355,889**
Individually impaired loans ***(total amount)***					
- not past due	6,088,803	12,424	-	-	**6,101,227**
- past due 30 days	-	16,115	-	-	**16,115**
- past due from 30 to 90 days	-	-	-	-	**-**
- past due from 91 to 180 days	2	-	-	-	**2**
- past due 181 – 360 days	3,427,722	3,622	-	103,909	**3,535,253**
- past due over 360 days	8,167,949	1,318,167	-	132,770	**9,618,886**
Total loans and impaired (total amount)	**17,684,476**	**1,350,328**	**-**	**236,679**	**19,271,483**
Provision for credit losses	**(9,549,584)**	**(553,249)**	**-**	**(208,605)**	**(10,311,438)**

The primary factors that the Bank considers in determining whether a loan is impaired are its overdue status and liquidity of related collateral, if any.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 11 LOANS AND ADVANCES TO CUSTOMERS (continued)

The fair value of collateral in respect of loans past due but not impaired and in respect of loans individually determined to be impaired at 31 December 2013 was as follows:

	Loans to legal entities	**Loans to private individuals, except for mortgages**	**Mortgages**
Fair value of collateral – loans past due but not impaired			
- Residential real estate	20,000	-	-
- Other real estate objects	6,127,192	-	-
- deposits	-	-	-
- Other assets	4,932,430	-	-
Fair value of collateral – individually impaired loans			
- Residential real estate	904,395	-	115,356
- Other real estate objects	18,471,030	-	1,044,937
- deposits	103,000	-	-
- Other assets	5,936,790	-	-
Total	**36,494,837**	**-**	**1,160,293**

The fair value of collateral in respect of loans past due but not impaired and in respect of loans individually determined to be impaired at 31 December 2012 was as follows:

	Loans to legal entities	**Loans to private individuals, except for mortgages**	**Mortgages**
Fair value of collateral – loans past due but not impaired			
- other real estate	5,283,734	-	2,481,388
- due to customers	-	-	-
- other assets	7,098,977	-	-
Fair value of collateral – individually impaired loans			
- residential real estate	2,663,375	-	-
- other real estate	15,634,361	1,809,900	28,400
- due to customers	26,550	-	-
- other assets	5,450,407	1,022,211	-
Total	**36,157,404**	**2,832,111**	**2,509,788**

The Bank's policy is to classify each loan as 'neither past due nor impaired' until specific objective evidence of impairment of the loan is identified.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 11 LOANS AND ADVANCES TO CUSTOMERS (continued)

The financial effect of collateral is presented by disclosing separately impact (i) on assets with collateral being equal or in excess of the book value of assets ("Assets with collateral value exceeding the loan balance"), and (ii) on assets with collateral being less than the book value of assets ("Assets with insufficient collateral").

The impact of collateral at 31 December 2013:

	Assets with collateral value exceeding the loan balance		**Assets with insufficient collateral**	
	Book value of asset (before provisions for impairment)	**Fair value of collateral**	**Book value of asset (before provisions for impairment)**	**Fair value of collateral**
	LVL	**LVL**	**LVL**	**LVL**
Loans to legal entities	51,068,911	123,382,271	9,074,511	4,046,571
Loans to individuals – consumer loans	4,909	25,975	1,221,941	618
Mortgage loans	1,329,054	2,173,054	236,785	28,400
Total	**52,402,874**	**125,581,300**	**10,533,237**	**4,075,589**

The impact of collateral at 31 December 2012:

	Assets with collateral value exceeding the loan balance		**Assets with insufficient collateral**	
	Book value of asset (before provisions for impairment)	**Fair value of collateral**	**Book value of asset (before provisions for impairment)**	**Fair value of collateral**
	LVL	**LVL**	**LVL**	**LVL**
Loans to legal entities	69,249,057	142,873,992	7,842,750	4,284,809
Loans to individuals, excluding mortgage loans	1,314,935	3,081,211	175,096	7,006
Mortgage loans	1,863,895	4,128,361	404,870	195,284
Reverse repurchase agreements (reverse repos)	2,291,143	2,408,945	-	-
Total	**74,719,030**	**152,492,509**	**8,422,716**	**4,487,099**

During 2013 rights to receive contractual cash flows from the loan amounting to LVL 2,157,898 were sold in non-recourse cession. The purchase price was LVL 515,000, thus creating loan write-off losses of LVL 1,642,898

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 12 FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT AND LOSS

	31.12.2013 LVL	31.12.2012 LVL
Latvian government securities	9,935,967	11,120,491
Non-OECD state government debt securities	2,034,899	2,312,350
Non-OECD region corporate debt securities	4,578,857	355,507
Unquoted securities	4,604	4,748
Quoted securities	1,226	826
	16,555,553	**13,793,922**

Analysis of securities by category as at 31 December 2013 and 31 December 2012 is presented below:

The following table discloses debt securities by issuers' ratings as at 31 December 2013 and 31 December 2012:

Rating	31.12.2013 Securities LVL	31.12.2013 %	31.12.2012 Securities LVL	31.12.2012 %
From A1 to A3	-	-	-	0.00%
From Baa1 to Baa3	9,935,966	60,02%	11,120,491	80.62%
From Ba1 to Ba3	4,172,559	25,20%	-	0.00%
From B1 to B3	11,978	0,07%	2,324,374	16.85%
Under B3	2,421,903	14,63%	306,588	2.22%
	16,542,406	99,92%	**13,751,453**	99.69%
Without rating	13,147	0,08%	42,469	0.31%
	16,555,553	**100%**	**13,793,922**	**100%**

NOTE 13 INTANGIBLE ASSETS

The following changes in the Bank's intangible assets took place during 2013 and 2012.

	Software 2013 LVL	Software 2012 LVL
Cost		
As at the beginning of the year	**866,019**	**850,920**
Additions	102,091	15,099
As at end of the year	**968,110**	**866,019**
Amortisation		
Accumulated amortisation at the beginning of the year	**717,303**	**591,374**
Charge for the year	88,101	125,929
Accumulated amortisation at the end of the year	**805,404**	**717,303**
Net book value at the beginning of the year	**148,716**	**259,546**
Net book value at the end of the year	**162,706**	**148,716**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 14 PROPERTY AND EQUIPMENT

The following changes in the Bank's property and equipment took place during the year ended 31 December 2013:

	Transport	Computers	Office equipment	Leasehold improvements	Total
	LVL	LVL	LVL	LVL	LVL
Cost					
31.12.2012	**16,750**	**497,040**	**408,906**	**70,932**	**993,628**
Additions	26,441	27,983	8,434	-	62,858
Disposals	-	(24,953)	(550)	-	(25,503)
31.12.2013	**43,191**	**500,070**	**416,790**	**70,932**	**1,030,983**
Depreciation					
31.12.2012	**16,750**	**445,784**	**288,790**	**17,196**	**768,520**
On disposals	**-**	(24,625)	(307)	**-**	(24,932)
Charge for 2012	881	33,480	56,049	4,298	94,708
31.12.2013	**17,631**	**454,639**	**344,532**	**21,494**	**838,296**
Net book value 31.12.2012	**-**	**51,256**	**120,116**	**53,736**	**225,108**
Net book value 31.12.2013	**25,560**	**45,431**	**72,258**	**49,438**	**192,687**

The following changes in the Bank's property and equipment took place during the year ended 31 December 2012:

	Transport	Computers	Office equipment	Leasehold improvements	Total
	LVL	LVL	LVL	LVL	LVL
Cost					
31.12.2011	**16,750**	**485,888**	**401,095**	**70,932**	**974,665**
Disposals	-	(13,851)	(1,881)	-	(15,732)
Additions	**-**	25,003	9,692	-	34,695
31.12.2012	**16,750**	**497,040**	**408,906**	**70,932**	**993,628**
Depreciation					
31.12.2011	**15,354**	**422,917**	**233,882**	**12,897**	**685,050**
On disposals	**-**	(13,731)	(1,881)	**-**	(15,612)
Charge for 2012	1,396	36,598	56,789	4,299	99,082
31.12.2012	**16,750**	**445,784**	**288,790**	**17,196**	**768,520**
Net book value 31.12.2011	**1,396**	**62,971**	**167,213**	**58,035**	**289,615**
Net book value 31.12.2012	**-**	**51,256**	**120,116**	**53,736**	**225,108**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 15 DUE TO CUSTOMERS

(a) Analysis of groups by customers

	31.12.2013 LVL	31.12.2012 LVL
Legal entities		
- current/ settlement accounts	241,655,527	259,628,920
- term deposits	10,226,661	13,532,642
Private individuals		
- current/ settlement accounts	10,650,390	6,896,214
- term deposits	17,032,335	24,830,455
Total customer accounts:	**279,564,913**	**304,888,231**
Sector profile:		
Private companies	251,702,114	271,834,977
Private individuals	27,682,725	31,726,669
Financial institutions	167,424	1,224,784
Non-profit institutions	4,368	98,522
Central government	8,282	3,279
Total customer accounts:	**279,564,913**	**304,888,231**

(b) Analysis by place of residence

Residents	20,340,483	24,864,343
Non-residents	259,224,430	280,023,888
Total customer accounts:	**279,564,913**	**304,888,231**

The average interest rate on term deposits in 2013 was 4.39% (2012: 4.20%) and the average interest rate on demand deposits was 0,48% (2012: 0.73%). All deposits have a fixed interest rate.

Economic sector concentration within customer accounts is as follows:

	2013		**2012**	
	LVL	**%**	**LVL**	**%**
Manufacturing	7,043,111	2.52	16,201,229	5,31
Building and real estate	4,064,885	1.45	14,029,662	4,60
Trade and commercial activities	103,920,933	37.17	123,090,266	40,37
Financial and insurance services	82,546,836	29.53	61,034,823	20,02
Transport and communications	45,599,923	16.31	35,880,644	11,77
Agriculture and food industries	1,201,222	0.43	2,067,015	0,68
Private individuals	27,682,725	9.90	31,726,669	10,41
Other	7,505,278	2.69	20,857,923	6,84
Total customer accounts	**279,564,913**	**100,0**	**304,888,231**	**100,0**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 16 BALANCES DUE TO BANKS

	31.12.2013 LVL	31.12.2012 LVL
Term deposit of Pivdennyi Bank	3,440	3,440
Other interbank borrowings	44,265	1,687,293
	47,705	**1,690,733**

NOTE 17 OTHER FINANCIAL LIABILITIES

Liabilities in clearance	347,271	2,808,226
Settlements on behalf of a closed bank	11,656	11,656
Cash in transit	22,725	74,820
Creditors settlements	52,764	74,185
	434,416	**2,968,887**

NOTE 18 DEFERRED INCOME AND ACCRUED EXPENSES

Accrued annual leave expenses	140,765	140,511
Accrual for guarantee fund and FCMC financing	162,974	257,110
State social security contributions to be paid	36,054	35,415
Accrued commission expenses	128,278	149,913
Other accrued expenses	72,639	78,542
	540,710	**661,491**

NOTE 19 DEFERRED INCOME TAX

The gross movement on the deferred income tax account is as follows:

	2013 LVL	2012 LVL
Deferred income tax (asset) / liability at the beginning of the reporting year	6,949	(6,628)
Deferred income tax change during the reporting year (see Note 8)	(20,521)	13,577
Deferred tax (asset) / liability at the end of the reporting year	**(13,572)**	**6,949**

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same taxation authority.

Deferred income tax has been calculated from the following temporary differences between assets and liabilities values for financial reporting and tax purposes:

	31.12.2013 LVL	31.12.2012 LVL
Deferred income tax liability:		
Temporary difference on fixed assets depreciation	12,951	33,256
Deferred income tax assets:		
Temporary difference on accruals for unused annual leave	(26,523)	(26,307)
Deferred tax (asset) / liability	**(13,572)**	**6,949**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 20 DERIVATIVE FINANCIAL INSTRUMENTS

The Bank uses the following derivative financial instruments: currency forwards – agreements on currency acquisition in future, currency swaps – agreements on exchange of one set of each cash flow for another.

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

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

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

	31.12.2013			**31.12.2012**		
	Contract / notional amount	**Fair value**		**Contract / notional amount**	**Fair value**	
		Assets	**Liabilities**		**Assets**	**Liabilities**
Currency swaps	9,525,093	146,767	(90,982)	26,582,699	110,680	(150,636)
Currency forwards	3,793,324	19,131	(9,079)	2,934,947	1,957	(6,583)
Total		**165,898**	**(100,061)**		**112,637**	**(157,219)**

The table below allocates the Bank’s derivative instruments future cash flows as at 31 December 2013:

	Up to 1 month LVL	**1 to 3 months LVL**	**Over 3 months LVL**	**Total LVL**
Derivatives settled on a gross basis				
Foreign exchange derivatives:				
- inflow	13,452,719	-	-	13,452,719
- outflow	(13,387,000)	-	-	(13,387,000)

The table below allocates the Bank’s derivative instruments future cash flows as at 31 December 2012:

	Up to 1 month LVL	**1 to 3 months LVL**	**Over 3 months LVL**	**Total LVL**
Derivatives settled on a gross basis				
Foreign exchange derivatives:				
- inflow	29,135,716	-	527,103	29,662,819
- outflow	(29,196,938)	-	(510,556)	(29,707,494)

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 21 SHARE CAPITAL

Issued and fully paid share capital as at 31 December 2013 was LVL 22,725,000 (2012: LVL 22,725,000)

On 6 November 2013 shareholder of the Bank Oleksandr Tambovcevs sold all his 200 000 shares to Drawnex Universal S.A.

As at 31 December 2013 the share capital consists of 22,725,000 ordinary shares with the nominal value of LVL 1 per share, of which 22,725,000 were shares with voting rights, total nominal value of EUR 22,725,000.

As at 31 December 2013 and 31 December 2012 shareholders of the Bank were:

	31.12.2013		31.12.2012	
	Paid-in share capital LVL	**% of total paid-in capital %**	**Paid-in share capital LVL**	**% of total paid-in capital %**
AB „Pivdenny" bank	18,599,670	81.85	18,599,670	81.85
Jurijs Rodins	2,100,000	9.24	2,100,000	9.24
DrawNex Universal S.A	1,100,000	4.84	900,000	3.96
Aztin corporation	500,000	2.20	500,000	2.20
Olegs Atayants	200,000	0.88	200,000	0.88
Vitālijs Medvedčuks	200,000	0.88	200,000	0.88
Oleksandrs Tambovcevs	-	-	200,000	0.88
Irina Veseluha	25,000	0.11	25,000	0.11
Haralds Āboliņš	220	-	220	-
Daiga Muravska	110	-	110	-
	22,725,000	**100.00**	**22,725,000**	**100.00**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 22 COMMITMENTS AND CONTINGENT LIABILITIES

Contingent liabilities

The following table discloses contingent liabilities:

	31.12.2013 LVL	31.12.2012 LVL
Warranties	2,399,357	6,016,694
	2,399,357	**6,016,694**

The Bank has issued warranties in the amount of LVL 2,399,357. These warranties are secured by deposits placed with the Bank or money resources in the security accounts or insurance policy of an insurance company.

Financial commitments

The following table discloses the contractual amounts of the Bank’s commitments to extend credit.

	31.12.2013 LVL	31.12.2012 LVL
Letters of credit	939,181	1,073,834
Commitments for trade cheques	226,078	325,996
Loans	24,865,023	17,770,705
	26,030,282	**19,170,535**

From which Bank’s commitments relating to lending were as follows:

Loan commitments	24,139,721	17,075,558
Undrawn credit lines	725,302	695,147
Total lending commitments	**24,865,023**	**17,770,705**

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

The lending commitments are denominated in the following currencies:

	31.12.2013 LVL	31.12.2012 LVL
USD	13,722,517	12,588,045
EUR	8,057,992	1,504,969
LVL	2,359,212	3,677,691
Total	**24,139,721**	**17,770,705**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 22 COMMITMENTS AND CONTINGENT LIABILITIES (continued)

Commitment under operating lease agreement

The Bank has entered into an operating lease agreement for its office premises. The lease agreement expires in June 2025. The non-cancellable lease liabilities payable within a year are LVL 308,344.

Where the Bank is the lessee, the future lease payments under concluded operating lease agreements are as follows:

	31.12.2013 LVL	31.12.2012 LVL
Up to 1 year	251,307	296,670
1 to 5 years	1,290,595	1,662,863
Over 5 years	1,746,562	2,710,821
Total	**3,288,465**	**4,670,354**

Assets pledged and restricted

As at year 2013 and 2012 the Bank had the following assets pledged:

	2013		2012	
	Assets pledged	**Related liabilities**	**Assets pledged**	**Related liabilities**
Balances due from banks	1,832,682	-	2,840,850	-
Other assets	1,907,304	-	-	-
Total	**3,739,986**	**-**	**2,840,850**	**-**

NOTE 23 CASH AND CASH EQUIVALENTS

	31.12.2013 LVL	31.12.2012 LVL
Cash and balances on demand with the Bank of Latvia	23,088,266	44,440,857
Due from banks with original maturity of 3 months or less	169,592,048	184,287,449
Due to banks with original maturity of 3 months or less	(47,705)	(1,690,733)
Total	**192,632,609**	**227,037,573**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 24 CAPITAL ADEQUACY

The Bank's calculation of the capital adequacy ratio according to the Finance and Capital Market Commission Guidelines as at 31 December 2013 has been set in the table below:

Description	**31.12.2013 LVL**
Tier 1	
- paid-in share capital	22,725,000
- audited retained earnings	2,957,394
- profit for the year	664,714
- intangible assets	(162,706)
Total Tier 1	**26,184,402**
Tier 2	
- subordinated capital	7,429,390
Total Tier 2	**7,429,390**
Capital base	**33,613,792**
Total capital requirements for credit and counterparty credit risks	
- standardised approach (SA)	10,358,775
Total capital requirement for position and foreign exchange risks	**998,921**
Total capital requirements for operational risk	
Basic index approach	1,069,517
Surplus of own funds	**21,186,579**
Total capital requirement	**12,427,213**
Capital adequacy ratio (%) *([Capital base]: [Capital requirement] x 8%)*	**21.64%**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 25 CURRENCY ANALYSIS

The following table provides the analysis of the Bank's assets, liabilities and shareholders' equity as well as off-balance sheet items outstanding as at 31 December 2013 by currency profile:

	USD LVL	EUR LVL	LVL LVL	Other LVL	Total LVL
Assets					
Cash and deposits with the Bank of Latvia	150,382	6,537,915	16,399,854	115	23,088,266
Balances due from banks	187,496,602	30,955,049	55,739	3,687,874	222,195,264
Loans and advances to customers	29,386,772	13,899,129	5,804,386	-	49,090,287
Financial assets at fair value through profit or loss	8,162,555	366,268	8,026,730	-	16,555,553
Intangible assets	-	-	162,706	-	162,706
Property and equipment	-	-	192,687	-	192,687
Deferred tax assets	-	-	13,572	-	13572
Other assets	2,524,322	230,895	126,283	494,896	3,376,396
Total assets	**227,720,633**	**51,989,256**	**30,781,957**	**4,182,885**	**314,674,731**
Liabilities and equity					
Balances due to banks	44,265	-	3,440	-	47,705
Due to customers	221,769,018	50,129,138	4,232,034	3,434,723	279,564,913
Other liabilities	517,692	62,119	368,852	26,463	975,126
Derivative financial instruments	-	-	100,061	-	100,061
Subordinated loan	7,639,818	-	-	-	7,639,818
Equity	-	-	26,347,108	-	26,347,108
Total liabilities and equity	**229,970,793**	**50,191,257**	**31,051,495**	**3,461,186**	**314,674,731**
Net long / (short) position on balance sheet	**(2,250,160)**	**1,797,999**	**(269,538)**	**721,699**	**-**
Off-balance sheet claims arising from foreign exchange					
Balances due from foreign exchange	8,069,365	5,332,326	-	51,029	13,452,720
Liabilities from foreign exchange	5,321,998	8,065,012	-	-	13,387,010
Net long / (short) position on foreign exchange	**2,747,367**	**(2,732,686)**	**-**	**51,029**	**65,710**
Net long / (short) position	**497,207**	**(934,687)**	**(269,538)**	**772,728**	**65,710**
As at 31 December 2012					
Total assets	**237,306,041**	**69,397,779**	**30,274,077**	**3,501,728**	**340,479,625**
Total liabilities and shareholders' equity	**250,980,577**	**54,862,134**	**32,473,669**	**2,163,245**	**340,479,625**
Net long / (short) position on balance sheet	**(13,674,536)**	**14,535,645**	**(2,199,592)**	**1,338,483**	**-**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 26 LIQUIDITY RISK AND ANALYSIS OF ASSETS AND LIABILITIES BY MATURITY PROFILE

The table below allocates the Bank's assets and liabilities to maturity groupings as at 31 December 2013 based on the time remaining from the balance sheet date to the contractual maturity dates:

	Overdue	Within 1 month	1 – 3 months	3 – 6 months	6 –12 months	1–5 years	Over 5 years and undated	Total
	LVL	LVL	LVL	LVL	LVL	LVL	LVL	LVL
Assets								
Cash and balances with the Bank of Latvia	-	23,088,266	-	-	-	-	-	**23,088,266**
Balances due from banks	-	173,762,157	14,468,403	10,616,257	22,215,447	1,133,000	-	**222,195,264**
Loans and advances to customers	6,033,815	1,296,140	3,705,034	3,994,120	17,985,241	15,586,374	489,563	**49,090,287**
Financial assets at fair value through profit or loss	-	16,555,553	-	-	-	-	-	**16,555,553**
Intangible assets	-	-	-	-	-	162,706	-	**162,706**
Property and equipment	-	-	-	-	-	-	192,687	**192,687**
Derivative financial instruments	-	165,898	-	-	-	-	-	**165,898**
Next period expenses	-	-	-	-	65,111	-	-	**65,111**
Deferred tax asset	-	-	-	-	13,572	-	-	**13,572**
Other assets	-	1,238,083	-	-	1,505,878	-	401,426	**3,145,387**
Total assets	**6,033,815**	**216,106,097**	**18,173,437**	**14,610,377**	**41,785,249**	**16,882,080**	**1,083,676**	**314,674,731**
Liabilities and equity								
Balances due to banks	-	47,705	-	-	-	-	-	**47,705**
Due to customers	-	243,401,042	5,361,093	3,362,761	16,978,488	10,289,279	172,250	**279,564,913**
Derivative financial instruments	-	100,061	-	-	-	-	-	**100,061**
Deferred income and accrued expenses	-	428,118	42,096	69,857	639	-	-	**540,710**
Other liabilities	-	434,416	-	-	-	-	-	**434,416**
Subordinated loan	-	4,428	-	-	-	1,030,000	6,605,390	**7,639,818**
Equity	-	-	-	-	-	-	26,347,108	**26,347,108**
Total liabilities and equity	**-**	**244,415,770**	**5,403,189**	**3,432,618**	**16,979,127**	**11,319,279**	**33,124,748**	**314,674,731**
Net liquidity	*6,033,815*	*(28,309,673)*	*12,770,248*	*11,177,759*	*24,806,122*	*5,562,801*	*(32,041,072)*	-
As at 31 December 2012								
Total assets	**-**	**254,962,396**	**4,675,470**	**25,344,856**	**30,836,850**	**24,001,557**	**658,496**	**340,479,625**
Total liabilities and equity	**-**	**262,156,784**	**6,161,215**	**5,349,559**	**17,224,087**	**19,484,480**	**30,103,500**	**340,479,625**
Net liquidity		*(7,194,388)*	*(1,485,745)*	*19,995,297*	*13,612,763*	*4,517,077*	*(29,445,004)*	-

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 26 LIQUIDITY RISK AND ANALYSIS OF ASSETS AND LIABILITIES BY MATURITY PROFILE (continued)

The table below allocates the Bank's financial liabilities on undiscounted cash flow bases as at 31 December 2013:

	Overdue	Within 1 month	1 – 3 months	3 – 6 months	6 –12 months	1–5 years	Over 5 years and undated	Total
	LVL	LVL	LVL	LVL	LVL	LVL	LVL	LVL
Balances due to banks	-	282,243	67,751	104,497	211,291	1,677,697	904,909	3,248,388
Due to customers	-	243,563,086	5,485,692	3,490,200	17,362,332	10,816,030	182,232	280,899,571
Other liabilities	-	434,416	-	-	-	-	-	434,416
Subordinated loan	-	59,151	120,188	118,063	192,805	1,224,456	6,613,358	8,328,021
Total liabilities	**-**	**244,339,076**	**5,673,631**	**3,712,760**	**17,766,428**	**13,718,183**	**7,700,499**	**292,910,576**

The table below allocates the Bank's financial liabilities on undiscounted cash flow bases as at 31 December 2012:

	Overdue	Within 1 month	1 – 3 months	3 – 6 months	6 –12 months	1–5 years	Over 5 years and undated	Total
	LVL	LVL	LVL	LVL	LVL	LVL	LVL	LVL
Balances due to banks	-	1,707,100	24,603	37,947	76,727	609,233	410,325	2,865,935
Due to customers	-	256,946,482	6,438,393	5,797,751	17,924,577	20,637,954	70,623	307,815,780
Other liabilities	-	2,975,836	-	-	-	-	-	2,975,836
Subordinated loan	-	12,793	20,355	30,532	61,065	488,520	4,616,189	5,229,454
Total liabilities	**-**	**261,642,211**	**6,483,351**	**5,866,230**	**18,062,369**	**21,735,707**	**5,097,137**	**318,887,005**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 27 RE-PRICING MATURITY OF ASSETS AND LIABILITIES

The table below allocates the Bank's assets and liabilities to maturity groupings as at 31 December 2013 based on the time remaining from the balance sheet date to the earlier of maturity and contractual re-pricing dates:

	Within 1 month	1–3 months	3–6 months	6–12 months	1–5 years	Over 5 years	Positions which are not sensitive to the interest rate risk	Total
	LVL	LVL	LVL	LVL	LVL	LVL	LVL	LVL
Assets								
Cash and balances with the Bank of Latvia	-	-	-	-	-	-	23,087,573	**23,087,573**
Balances due from banks	176,087,082	11,845,000	9,270,000	15,450,000	-	-	9,543,182	**222,195,264**
Loans and advances to customers	7,912,954	4,757,417	7,638,930	17,111,492	11,103,539	485,037	-	**49,009,369**
Financial assets at fair value through profit or loss	-	-	5,003,925	-	10,645,146	900,652	5,830	**16,555,553**
Intangible assets	-	-	-	-	-	-	162,706	**162,706**
Property and equipment	-	-	-	-	-	-	192,687	**192,687**
Deferred tax expenses	-	-	-	-	-	-	13,572	**13,572**
Other assets	-	-	-	-	-	-	3,376,396	**3,376,396**
Total assets	**184,000,036**	**16,602,417**	**21,912,855**	**32,561,492**	**21,748,685**	**1,385,689**	**36,463,557**	**314,674,731**
Liabilities								
Balances due to banks	-	-	-	-	-	-	47,705	**47,705**
Due to customers	40,819,025	2,643,065	2,037,096	10,072,292	9,102,503	171,585	214,454,544	**279,300,110**
Other liabilities	-	-	-	-	-	-	1,344,418	**1,344,418**
Subordinated loan	-	-	-	-	1,030,000	6,605,390	-	**7,635,390**
Total liabilities	**40,819,025**	**2,643,065**	**2,037,096**	**10,072,292**	**10,132,503**	**6,776,975**	**215,846,667**	**288,327,623**
Equity	**-**	**-**	**-**	**-**	**-**	**-**	26,347,108	**26,347,108**
Total liabilities and equity	**40,819,025**	**2,643,065**	**2,037,096**	**10,072,292**	**10,132,503**	**6,776,975**	**242,193,775**	**314,674,731**
On balance sheet interest sensitivity analysis	*143,181,011*	*13,959,352*	*19,875,759*	*22,489,200*	*11,616,182*	*(5,391,286)*	*(205,730,218)*	-
As at 31 December 2012								
Total assets	**145,534,080**	**10,421,549**	**29,485,624**	**21,903,048**	**24,505,786**	**1,178,486**	**107,451,052**	**340,479,625**
Total liabilities and equity	**45,859,531**	**4,525,572**	**4,117,146**	**9,032,803**	**15,626,425**	**4,421,106**	**256,897,042**	**340,479,625**
On balance sheet interest sensitivity analysis	*99,674,549*	*5,895,977*	*25,368,478*	*12,870,245*	*8,879,361*	*(3,242,620)*	*(149,445,990)*	-

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 28 RELATED PARTY TRANSACTIONS

Parties are considered to be related if one party has the ability to control the other party or exercise 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, their close relatives and companies in which they have a controlling interest as well as associated companies.

The balances in respect of operations with related parties are as follows as at 31 December 2013:

	Enterprises under the control of related parties	**Other related parties**
Undrawn credit lines	**52**	**24,336**
Assets under management	**2,883,611**	**-**

Total amounts of loan commitments issued to and repaid by related parties during 2013 are as follows:

	Shareholders with significant control	**Enterprises under the control of related parties**	**Other related parties**
Issued to related parties	11,252,824,307	178,092	148,738
Repaid by related parties	11,296,624,272	173,518	162,872

Operations with the related parties were as follows as at 31 December 2013:

	Shareholders with significant control	**Enterprises under the control of related parties**	**Other related parties**
Total loans and advances (interest rate on agreement: 5,7-24%)	39,636,951	1,789,385	6,321
Correspondent account	1,613,295	-	-
Due to customers (interest rate: 0.10-5,0%)	-	14,626,555	1,353,500
Subordinated loan	5,062,687	515,100	-
Vostro account	3,440	-	-

Income and expense from operations with related parties during 2013 were as follows:

	Shareholders with significant control	**Enterprises under the control of related parties**	**Other related parties**
Interest income	4,267,211	148,918	1,402
Interest expenses	(299,165)	(648,017)	(60,998)
Fee and commission income	-	1,432	666
Fee and commission expense	(4,820)	-	-
Administrative and other operating expenses	(14,171)	-	-

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 28 RELATED PARTY TRANSACTIONS (continued)

The balances in respect of operations with related parties are as follows as at 31 December 2012:

	Enterprises under the control of related parties	**Other related parties**
Undrawn credit lines	**53**	**5,414**

Total amounts of loan commitments issued to and repaid by related parties during 2012 are as follows:

	Shareholders with significant control	**Enterprises under the control of related parties**	**Other related parties**
Issued to related parties	14,973,544,949	-	82,258
Repaid by related parties	14,913,600,363	-	85,341

Operations with the related parties were as follows as at 31 December 2012:

	Shareholders with significant control	**Enterprises under the control of related parties**	**Other related parties**
Total loans and advances (interest rate on agreement: 2-24%)	83,609,478	1,844,719	20,576
Correspondent account	2,699,528	-	-
Due to customers (interest rate: 3,65-8.5%)	-	13,185,884	1,373,238
Derivatives	1,343	-	-
Subordinated loan	1,766,523	-	-
Vostro account	3,440	-	-

Income and expense from operations with related parties during 2012 were as follows:

	Shareholders with significant control	**Enterprises under the control of related parties**	**Other related parties**
Interest income	6,000,315	154,966	1,226
Interest expenses	(286,764)	(422,339)	(60,422)
Fee and commission income	-	541	601
Fee and commission expense	(6,156)	-	-
Administrative and other operating expenses	(15,819)	-	-

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 28 RELATED PARTY TRANSACTIONS (continued)

Remuneration to key management personnel is disclosed below:

	2013 LVL	2012 LV
Short-term benefits:		
- Salaries	208,599	209,249
Pension benefits:		
- Expenses to the State Pension Insurance	49,366	50,029
Total	**257,965**	**259,278**

NOTE 29 FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES

Fair value of financial instruments is such amount of cash, for which the asset can be sold or liability settled between two unrelated, independent parties based on generally accepted terms and conditions. The Bank discloses information on fair values of assets and liabilities in such a way as to enable its comparison with book values.

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). When the price for these assets is not readily available, fair value is determined based on prices available in less active markets – such approach is used for several debt instruments.

Various methods are used by the Bank for those financial assets, which are not quoted in the market and for which no prices for similar quoted instrument are available. While determining fair value of these financial instruments, the Bank uses models based on assumptions and estimates on possible financial performance of investment object, as well as industry in which it operates, inherent risks and geographic segment in which investment object is operating.

Fair value of derivative financial instruments is determined based on discounted cash flow models with all parameters used being directly observable in the market.

Other assets and liabilities for which fair value is disclosed, except for loans and advances to customers, the Bank assumes that fair value equals book values. This assumption relates also to deposit placements and current accounts. Fair value of loans is determined via discounting expected cash inflows with the discount rate, which is determined taking into account money market rates at the end of the reporting year and interest rates for loans.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 29 FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES (continued)

The table below shows assets and liabilities valued at fair value by book values and fair values as at 31 December 2013 and 31 December 2012:

	Book value LVL	31.12.2013 Fair value LVL	Book value LVL	31.12.2012 Fair value LVL
Assets valued at fair value				
Derivative financial instruments	165,898	165,898	112,637	112,637
Financial assets at fair value through profit or loss	16,555,553	16,555,553	13,793,922	13,793,922
Total assets valued at fair value	**16,721,451**	**16,721,451**	**86,736,868**	**93,606,086**
Liabilities valued at fair value				
Derivative financial instruments	100,061	100,061	157,219	157,219
Total liabilities valued at fair value	**100,061**	**100,061**	**157,219**	**157,219**

The table below shows assets and liabilities valued at amortised cost by book values and fair values as at 31 December 2013 and 31 December 2012:

	Book value LVL	31.12.2013 Fair value LVL	Book value LVL	31.12.2012 Fair value LVL
Assets valued at amortised cost				
Cash and balances with the Bank of Latvia	23,088,266	23,088,266	44,440,857	44,440,857
Balances due from banks	222,195,264	222,195,264	207,381,802	207,381,802
Loans and advances to customers	49,090,287	53,672,069	72,830,309	79,699,527
Total assets valued at amortised cost	**294,373,817**	**298,955,599**	**324,652,968**	**331,522,186**
Liabilities valued at amortised cost				
Balances due to banks	47,705	47,705	1,690,733	1,690,733
Due to customers	279,564,913	279,564,913	304,888,231	304,888,231
Subordinated loan	7,639,818	7,639,818	4,423,721	4,423,721
Total liabilities valued at amortised cost	**287,252,436**	**287,252,436**	**311,002,685**	**311,002,685**

When determining fair values of assets and liabilities, the Bank is using various sources of fair value, which are grouped into three categories based of following hierarchy:
Category 1 – quoted market prices in an active market;
Category 2 – models to determine fair value using data directly observable in the market;
Category 3 – other methods for determining fair value using data, which is not directly observable in the market.

Instruments within Category 1 include highly liquid assets and standard derivative financial instruments traded on the stock exchange.
Instruments within Category 2 include assets, for which no active market exists, such as over the counter derivative financial instruments and currency swaps agreements.
Category 3 instruments are all other assets and liabilities, as well as loans.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 29 FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES (continued)

The table below specified analysis by fair value categories as at 31 December 2013 and 31 December 2012 (based on carrying amounts):

	31.12.2013			31.12.2012		
	Category 1	**Category 2**	**Category 3**	**Category 1**	**Category 2**	**Category 3**
Assets valued at fair value						
Derivative financial instruments	-	165,898	-		112,637	
Financial assets at fair value through profit or loss	16,555,553	-	-	13,793,922	-	-
Total assets valued at fair value	**16,555,553**	**165,898**	-	**13,793,922**	**112,637**	**-**
Assets valued at amortised cost						
Cash and balances with the Bank of Latvia	23,088,266	-	-	44,440,857	-	-
Balances due from banks	222,195,264	-	-	207,381,802	-	-
Loans and advances to customers	-	-	49,090,287	-	-	72,830,309
Total assets valued at amortised cost	**245,283,530**	-	**49,090,287**	**251,822,659**	**-**	**72,830,309**
Liabilities valued at fair value						
Derivative financial instruments	-	100,061	-	-	157,219	-
Total liabilities valued at fair value	**-**	**100,061**	**-**	**-**	**157,219**	**-**
Liabilities valued at amortised cost						
Balances due to banks	47,705	-	-	1,690,733	-	-
Due to customers	279,564,913	-	-	304,888,231	-	-
Subordinated loan	7,639,818	-	-	4,423,721	-	-
Total liabilities valued at amortised cost	**287,252,436**	**-**	**-**	**311,002,685**	**-**	**-**

NOTE 30 TAXES

	Balance 31.12.2013	**Calculated in 2013**	**Returned from the budget**	**Paid in 2013**	**Balance 31.12.2013**
	LVL	**LVL**	**LVL**	**LVL**	**LVL**
Corporate income tax*	-	858,814	**-**	(858,814)	-
State compulsory social insurance contributions	-	616,254	**-**	(616,254)	-
Personal income tax	(1,787)	356,261	**-**	(356,843)	(2,369)
Value added tax	(44,264)	(9,548)	64,867	(22,961)	(11,906)
(Overpaid)	**(46,051)**				**(14,275)**
Liabilities	**-**				**-**

* CIT calculated and paid includes the amount of tax withheld abroad – LVL 858,814.

The tax authorities have the right to inspect the tax computations for the last three taxation years. The Bank's management is not aware of any circumstances which may give rise to a potential material liability in this respect.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 31 SUBORDINATED LOAN

On 23 August 2011 the Bank signed an agreement with Venture Resource Investments LTD receiving subordinated loan in amount of USD 2,000,000 maturing in 2019. At 31 December 2013 interest rate for subordinated loan was 8%.

On 9 December 2011 the Bank signed an agreement with Aleksey Fedorichev receiving subordinated loan in amount of USD 2,000,000 maturing in 2018. As at 31 December 2013 interest rate for subordinated loan was 7%.

On 8 June 2012 the Bank signed an agreement with Fortum Trade Services LTD receiving subordinated loan in amount of USD 1,000,000 maturing in 2019. As at 31 December 2013 interest rate for subordinated loan was 7%.

On 20 June 2012 Bank signed an agreement with Pivdennyi Bank receiving subordinated loan in amount of USD 2,000,000, on 15 August – USD 5,000,000 and on 7 September – USD 5,500,000. On 11 December 2012 after receiving of approval from FCMC the agreements for subordinated loan in amounts of USD 2,000,000, USD 5,000,000 and USD 2,174,000 (part of USD 5,500,000) were cancelled and the assets were used in the increase of the Bank’s share capital for the amount LVL 5,000,000. As at 31 December 2013 the balance of the subordinated loan of Pivdennyi Bank comprise USD 3,326,000 maturing in 2020. As at 31 December 2013 interest rate for subordinated loan was 8.5 %.

On 30 April 2013 the Bank signed an agreement with Pivdennyi Bank receiving subordinated loan in amount of USD 1,000,000 maturing in 2021. As at 31 December 2013 interest rate for subordinated loan was 8.0%.

On 22 may 2013 the Bank signed an agreement with Pivdennyi Bank receiving subordinated loan in amount of USD 1,500,000 maturing in 2021. As at 31 December 2013 interest rate for subordinated loan was 8.0%.

On 5 June 2013, Bank signed an agreement with the Bank on a subordinated loan Pivdenny receipt of USD 4,000,000 maturing in 2021. As at 31 December 2013 interest rate for subordinated loan was 8.0%.

As at 31 December 2013 subordinated loans amounted to total of LVL 7,639,818 (31.12.2013: LVL 4,423,721).

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 32 SUBSEQUENT EVENTS

In the first quarter of 2014 political and economic system in Ukraine became unstable and attracted attention of the whole world. On 21 November 2013 president of Ukraine announced his refusal to sign Association Agreement with European Union. This announcement caused wide protests from citizens of Ukraine, as a result of which civil unrest in Kiev arose. Situation was further deteriorated by ignorance of protests and application of military force on public, as well as decision of Ukrainian government on transaction with the government of Russian Federation on sale of Ukrainian government bonds amounting to 15 billion USD. In the end of January 2014 president of Ukraine agreed to change the prime minister, however, within short period of time he left the country and lost trust of the Cabinet of Ministers.

On 26 February 2014 the newly formed majority coalition of the Parliament voted for new prime minister and new Cabinet of Ministers. New Cabinet of Ministers initiated immediate dialogue with International Monetary fund in order to ensure availability of additional financing and avoidance of possible default on borrowings, as well as undertook work on signing process of Association agreement. After formation of new Cabinet of Ministers in Ukraine, Russia ceased its financial support to Ukraine and Moody's decreased rating of Ukrainian government bonds from Caa1 to Caa2 with negative outlook. During first two months of 2014 Ukrainian hrivna experiences significant drop in value, while Central Bank of Ukraine limited foreign currency purchase deals in Ukrainian banks.

In the beginning of March 2014 it is hard to predict the impact of political and economic crisis in Ukraine on the further development of the Bank, as there is no certainty about future political and economic development of Ukraine, moreover, stabilisation of the situation is currently delayed by events in Crimea.

The following table indicates total exposition of the Bank in Ukraine as at 31 December 2013 and as at 28 February 2014:

	31.12.2013 thousand EUR	28.02.2014 thousand EUR
Balance sheet assets subject to the country risk:		
Balances due from banks	98,645	87,518
Loans issued	38,232	38,141
Financial assets at fair value through profit or loss	2,895	-
Total	**140,021**	**125,659**

	31.12.2013 thousand EUR	28.02.2014 thousand EUR
Off-balance sheet items subject to country risk:		
Off-balance sheet commitments to clients	13,179	16,372
Total	**13,179**	**16,372**