JSC Aizkraukles banka public quarterly report for the period ended on 31 December 2010

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Bank's managements report

Ladies and Gentlemen,

Dear Shareholders, Customers and Business Partners of Aizkraukles Banka,

The Group's and the Bank's management is highly satisfied with the results for the year 2010. The Group's and the Bank's financial performance has improved significantly, in line with fully restored investor confidence the deposit growth has been outstanding, and high level of liquidity and a solid capital adequacy ratio have been maintained all through 2010. The Group and the Bank have over fulfilled the financial objectives set for the reporting period.

Over the year 2010, the volumes in the entire core business lines of the Group have enlarged substantially – tailor-made services to affluent individuals and their businesses, asset management, and investment operations. We are proud to announce that the Bank has become the largest privately-owned bank in Latvia.

Global economy still was on the track of recovery in 2010. However, growth rates varied considerably across the globe. Most rapid growth was observed in developing countries of Asia, whereas the economic development in USA and Japan decelerated, whilst European countries, especially, Germany, performed unexpectedly well. Nevertheless, several European Union member states, Greece, Ireland, Portugal and Spain in particular, found themselves in financial struggles.

In Latvia, the lowest point of economic downturn passed in 2009 and macroeconomic indicators were on the upward trend since the very beginning of 2010. On a quarterly basis the seasonally adjusted GDP growth ranged between 0.3 – 1.4% in 2010. In the third quarter of 2010, an increase of GDP on the annual basis was recorded as well, reaching a 3.7% figure at the year-end. Over the first three quarters of 2010, the production output increased by 13% and volume of exports – by 29%. Retail indicators have also improved. The decline in unemployment rate is gradual, but consistent. The government of Latvia foresees a 3.3% and 4.0% GDP growth in 2011 and 2012, respectively.

Yet another positive sign appeared in late in 2010, when international rating agency Standard & Poor's raised the Republic of Latvia's foreign and local currency long-term sovereign credit rating to 'BB+' from 'BB'. The outlook is stable. The rating changes state that the Latvian economy is rebalancing quickly, though public debt remains at moderate levels. We estimate the rating action to be a material appraise of the country's creditworthiness, as well as a signal for investors confirming that past economic imbalances have rapidly unwound.

Consistently applying deliberative business strategy, performing all the scheduled tasks and operational optimisations in a concert effort, the financial performance of the Group and the Bank was enhanced in 2010:

- The amount of customer deposits rose at an exceptional pace (a 43.6% increase for the Bank). Aizkraukles banka contributed one fourth or 25.5% of the total deposit growth within the Latvian banking industry in the year 2010.
- Operating efficiency of the Bank was boosted (operating profit before allowances for credit losses equalled LVL 46.2 million, which is 17% above that in 2009);
- The Bank ensured high liquidity ratio of 68.1% and capital adequacy ratio of 12.45%, as at 31 December 2010;
- The Bank's share capital was increased by LVL 6.5 million.

The major event of 2010 was the issue of the Bank's ordinary shares completed in July 2010. There were 10 000 shares issued in addition to those 100 000 that constituted the Bank's share capital until then. Afterwards, the new shares represent 9.09% of the total Bank's share capital. The shares were sold at a price of LVL 650. Two thirds of the new issue were obtained by the current shareholders, management and employees of the Bank as well as those *private banking* customers, who are Latvian residents. The rest of the shares were obtained by non-resident customers, mainly private individuals. Although this was a private issue targeted at narrow circle of participants, the total volume of paid-up applications surpassed LVL 9 million – it was a 40% oversubscription, therefore several bids were satisfied partially. As a result of issuance, the Bank obtained 30 new shareholders.

Both the successful share issuance and non-resident deposit growth in 2010 show customer reliance on the Aizkraukles banka and the Latvian financial system in general.

Considering the course of events in Latvia and across the globe, the management of the Group and the Bank is confident that Aizkraukles banka is in a strong position to continue successfully in operational existence and fully meet its obligations in the foreseeable future.

These financial statements have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union and give a true and fair view of the assets, liabilities, and financial position of the Bank and the Group as of 31 December 2010 and 31 December 2009, and results of their operations, changes in the shareholders' equity and cash flows for the years 2010 and 2009.

As of the end of 2010, the following subsidiaries of the Bank constituted the Group: brokerage joint stock company AB.LV Capital Markets, investment management joint stock company AB.LV Asset Management, SIA AB.LV Private Equity Management, KS AB.LV Private Equity Fund 2010, SIA AB.LV Corporate Services, KS AB.LV Transform Partnership, SIA AB.LV Transform 1, AS AB Konsultācijas, SIA New Hanza City, and SIA Elizabetes 21a.

Financial results

As at 31 December 2010, total assets of the Bank amounted to LVL 1.38 billion.

Substantial deposit increase was observed all through 2010. Over the year deposits grew by LVL 379 million or 43.6%, thus reaching the total volume of LVL 1.25 billion. This figure significantly exceeds yet ambitious sales targets set in the beginning of year 2010. For the second consecutive year the Bank ranks number one in the Latvian banking industry in terms of corporate deposit amount.

Following the strategic goals, the Bank continued reduction of its mortgage loan portfolio. In the course of 2010, the mortgage loan portfolio was decreased by LVL 18.3 million and amounted to LVL 408 million at the year-end.

With an average balance being LVL 217 million, the Bank's debt securities portfolio earned a solid annual yield of 5.53% in 2010. The Bank's securities portfolio is mainly composed of debt securities issued by central governments of OECD countries, credit institutions and corporate companies of other countries.

The share of non- interest income in the total operating income before allowances for credit losses enlarged notably from 50% to 55% during the reporting period. In monetary terms, non- interest income increased by 27% in 2010. Such a remarkable outcome resulted from heightened customer activity, primarily in those areas being commission and fee based. In 2010, an all time high was observed in terms of number of commission related transactions, which means the Bank has not only regained the level of its pre-crisis operations, but even exceeded it.

The Bank's operating income before allowances for credit losses comprised LVL 46.2 million for the year 2010. Having a prudent and conservative approach to loan portfolio quality assessment in place, the Bank proceeded with additional allowances for credit losses. As at 31 December 2010, total allowances for credit losses equalled LVL 65.4 million. In the period from 2007 to 2010, the Bank has provided allowance in the amount of LVL 86.2 million in the aggregate. Given consistent implementation of the above allowance policy, the Bank recorded a loss of LVL 6.9 million in 2010.

As of 31 December 2010, the Bank's shareholders equity amounted to LVL 75.4 million.

Improvement of services

During the reporting period in line with the aforeset course of action the Bank established a subsidiary company for risk capital investment fund management – SIA AB.LV Private Equity Management. Accordingly the fund itself was created for private capital investment, hence named AB.LV Private Equity Fund 2010.

The fund has been started still at the time when economy of the country has insufficient capacity to attract investment capital and funding provided by banks remains suspended. Thus the Bank emphasizes the inclination to trigger financing of entrepreneurs in Latvia. The venture would foster the businesses to switch the direction of the development curve upwards and help the economy to regain the sustainable permanent growth.

Last year AB.LV Private Equity Fund 2010 obtained 60% of the share capital in limited liability companies “Bio Future” and “Gas Stream”. In the neighbourhood of Vaiņode the companies have arrangements to build two biogas plants with the total electricity production capacity of 2MW.

Moreover, at the end of 2010, in a form of a structured deal AB.LV Private Equity Fund financed an acquisition of 11.38% stake in the leading Latvian pharmaceutical company AS Grindeks.

In the reporting period, the Bank continued to issue subordinated bonds according to the programme implemented back in 2008. The Bank’s third issue of subordinated bonds was successfully completed in September 2010. The deal closed with a 16% oversubscription. The bank issued 200 000 bonds in total, with each bond’s par value being equal to USD 100. The overall amount of the bond issue totalled USD 20 million. The initial two subordinated bond issues of the Bank took place in 2008. The bonds were denominated in US dollars and euros, the total amount being equal to USD 20 million and EUR 12.5 million accordingly. Considering great interest of the Bank’s customers in acquiring the bonds, it is planned to continue issuing subordinated bonds in future.

Pursuant to amendments to the Republic of Latvia Immigration Law, starting from 1 July 2010, the Bank’s foreign customers are offered new service – assistance in receiving Latvian residence permit. The residence permit allows for non-EU citizens to reside in the Republic of Latvia pro tempore or permanently. The aforementioned service has already become rather popular, and it is rendered by the Bank’s subsidiary SIA AB.LV Corporate Services.

In 2010, the network of the Group’s representative offices abroad expanded. In December, a new representative office of AS AB Konsultācijas was registered in Russia, in Yekaterinburg. The representative office will begin its operations in this momentous region of Russia in 2011.

Currently, the Group has representative offices in Azerbaijan (Baku), Belarus (Minsk), Kazakhstan (Almaty), Russia (Moscow, St. Petersburg, and Yekaterinburg), Tajikistan (Dushanbe), Uzbekistan (Tashkent), and Ukraine (Kiev, with its branch in Odessa). The main task of the representative offices is to provide information about the Group and the Bank and their services, alongside promoting international economic cooperation in various areas of business. In the coming years the Group will continue to broaden its network of representative offices abroad.

The Group’s and the Bank’s plans and intentions for 2011

The core objectives for 2011, likewise the reporting period, will be to ensure uttermore expansion of the Group’s and the Bank’s business and boost profitability, whilst developing and enhancing operational risk management framework.

On the ground of pace of economic recovery found at the Group’s and the Bank’s target markets and limited need for additional allowances, the Bank is in a position to increase the issuance of commercial loans in 2011.

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In 2011, the Group's and the Bank's management will also focus on restructuring of the loans issued under the Bank's mortgage lending programmes and loan portfolio quality.

Deposits are expected to grow by 15% in 2011.

Taking into account the foreseen increment in commercial loan portfolio, deposits and commission and fee income, the management of the Group and the Bank is confident that in 2011 Aizkraukles Banka will run at a profit and will be successful at broadening its business and boosting its efficiency. Return on equity (ROE) is anticipated to advance to a 15% level.

Bank for society

In 2010, Aizkraukles Banka continued supporting various socially important projects.

Provided financial assistance of Aizkraukles Banka, *Art Deco – the fashion style of interwar period* exhibition was opened in Riga Museum of Decorative Arts and Design, where dress collection of famous fashion historian Alexandre Vassiliev was presented. It was the second time Alexandre Vassiliev's dress collection has been exhibited in Riga. The first exhibition, *Victorian Fashion*, took place in 2009 and was exceptionally popular among visitors. That exhibition has also been funded by our Bank.

Traditionally, Aizkraukles Banka provided support to the Republic of Latvia embassies abroad in arranging the commemoration of Proclamation Day of the Republic of Latvia. This year, the Bank endowed celebration events in the Republic of Latvia embassies in Russia, Kazakhstan, and Azerbaijan.

It its turn, AB.LV Sabiedriskā labuma fonds in 2010 had contributed to nine contemporary art exhibitions in Latvia that had different concepts, but were equally outstanding. The Fund has been supporting contemporary art exhibitions since 2007. During the last four years, the Fund allocated more than LVL 100 000 to arranging contemporary art exhibitions.

In the last year, holdings of the Latvian Contemporary Art Museum, which are compiled with the Bank's assistance, have been supplemented. Two new paintings by Imants Lancmanis were purchased. Therefore, the holdings now comprise 10 pictures by Imants Lancmanis, and the total number of the works of art is 96. The Bank's total input in supplementing and popularizing the contemporary art collection exceeds LVL 230 000.

Also, in August 2010, the Bank held AB.LV Charity Golf Tournament 2010 for the Bank's customers, inviting them to participate in "Skolas soma" fund drive, making donations for buying school goods for junior schoolchildren from low-income families. The funds raised during the tournament were used to equip 52 schoolchildren.

At the end of the year, the Bank together with AB.LV Sabiedriskā labuma fonds held a traditional fund drive "Palīdzēsim bērniem dzirdēt!". The funds raised during this campaign will be used to supply children with necessary hearing devices.

We express our gratitude to the Bank's shareholders and customers for their loyalty and confidence and to the Bank's employees for their contribution to the Bank's development!

Chairman of the Council	Aleksandrs Bergmanis
Chairman of the Board	Ernests Bernis

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General information

The JSC Aizkraukles banka (hereinafter referred to as the Bank) was registered as a joint stock company in Aizkraukle, Republic of Latvia on 17 September 1993, under reg. No 50003149401. At present, the legal address of the Bank is 23 Elizabetes Street, Riga.

The Bank operates in accordance with the legislation of the Republic of Latvia and the licence issued by the Bank of Latvia that allows the Bank to render all the financial services specified in the Law on Credit Institutions.

The Bank’s main scope of activity is investment services, settlement products, and asset management.

The Group and the Bank operate the central office and two lending centres in Riga, as well as three foreign representation offices in Azerbaijan - Baku, in Belarus- Minsk, in Kazakhstan - Almaty, in Russia – Moscow, St. Petersburg and Jekaterinburg, in Ukraine - Kyiv with its branch in Odessa, in Uzbekistan - Tashkent and Tajikistan – Dushanbe.

The Group's and the Bank's financial statements, who prepared in consistently applying IFRS as adopted in the EU and the FCMC Regulations on the Preparation of Annual Reports and Consolidated Annual Reports of Banks, Investment Brokerage Companies, and Investment Management Companies, were audited by Ernst & Young Baltic SIA, unified registration number Nr. 40003593454, Latvijas Republika, Muitas str.1.

This quarterly report is prepared in accordance with the Regulations on Preparation of Public Quarterly Reports for Banks approved by the Financial and Capital Market Commission for the purpose of providing information on the financial standing and performance indicators of the Group and the Bank.

Financial statements are reported in thousands of lats (LVL ‘000), unless otherwise stated.

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Members of the consolidation group as at 31 December 2010

Name of the business company	Registration number	Registration address	Type of activities*	Interest in share capital (%)	Share of voting rights (%)	Motivation for inclusion in the group**
IPAS "AB.LV Asset Management"	40003814724	Elizabetes iela 23, Rīga, LV-1010	IPS	100	100	MS
IBAS "AB.LV Capital Market"	40003814705	Elizabetes iela 23, Rīga, LV-1010	IBS	100	100	MS
AS "AB Konsultācijas"	40003540368	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
SIA "AB.LV Corporate Services"	40103283479	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
KS "AB.LV Transform Partnership"	40103260921	Elizabetes iela 23, Rīga, LV-1010	CFI	99.9997	99.9997	KS
SIA "AB.LV Transform Investments"	40103191969	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
SIA "AB.LV Transform 1"	40103193211	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
SIA "AB.LV Transform 2"	40103193033	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
SIA "AB.LV Transform 3"	40103193067	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
SIA "AB.LV Transform 4"	40103210494	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
SIA "AB.LV Transform 6"	40103237323	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
SIA "AB.LV Transform 7"	40103237304	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
SIA "AB.LV Transform 8"	40103240484	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
SIA "AB.LV Transform 9"	40103241210	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
SIA "AB.LV Transform 10"	50103247681	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
SIA "AB.LV Transform 11"	40103258310	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
SIA "AB.LV Transform 12"	40103290273	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
SIA "AB.LV Transform 13"	40103300849	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
SIA "AB.LV Transform 14"	50103313991	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
SIA "AB.LV Transform 15"	40103344858	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
SIA "Elizabetes 21a"	50003831571	Elizabetes iela 23, Rīga, LV-1010	CKS	91.6	91.6	MS
SIA "New Hanza City"	40103222826	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
SIA "AB.LV Private Equity Management"	40103286757	Elizabetes iela 23, Rīga, LV-1010	CKS	100	100	MS
KS "AB.LV Private Equity Fund 2010"	40103307758	Elizabetes iela 23, Rīga, LV-1010	CFI	100	100	KS
SIA "Gas Stream"	42103047436	Elizabetes iela 23, Rīga, LV-1010	CKS	60	60	MS
SIA "Bio Future"	42103047421	Elizabetes iela 23, Rīga, LV-1010	CKS	60	60	MS

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Shareholders and groups of related shareholders of the bank as at 31 December 2010

Shareholders	Number of voting shares	Par value of shares in lats	% of the total paid-in the Bank's share capital	Paid-in the Bank's share capital in lats
Ernests Bernis group of related shareholders				
Ernests Bernis	*46,212*	*150*	*42.01*	*6,931,800*
Nika Berne	*1,030*	*150*	*0.94*	*154,500*
Total of group	47,242		42.95	7,086,300
Oļegs Fiļs	47,241	150	42.95	7,086,150
Other shareholders	15,517	150	14.10	2,327,550
Total	**110,000**		**100.00**	**16,500,000**

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The council and the board

The Council of the Bank:

Chairman of the Council:
Aleksandrs Bergmanis

Deputy Chairman of the Council:
Jānis Krīgers

Member of the Council:
Igors Rapoports

The Board of the Bank:

Chairman of the Board:
Ernests Bernis – *Chief Executive Officer (CEO)*

Deputy Chairman of the Board:
Oļegs Fiļs – *Deputy Chief Executive Officer (dCEO)*

Members of the Board:
Aleksandrs Pāže – *Chief Compliance Officer (CCO)*
Edgars Pavlovičs – *Chief Risk Officer (CRO)*
Māris Kannenieks – *Chief Financial Officer (CFO)*
Rolands Citajevs – *Chief IT Officer (CIO)*
Vadims Reinfelds – *Chief Operating Officer (COO)*

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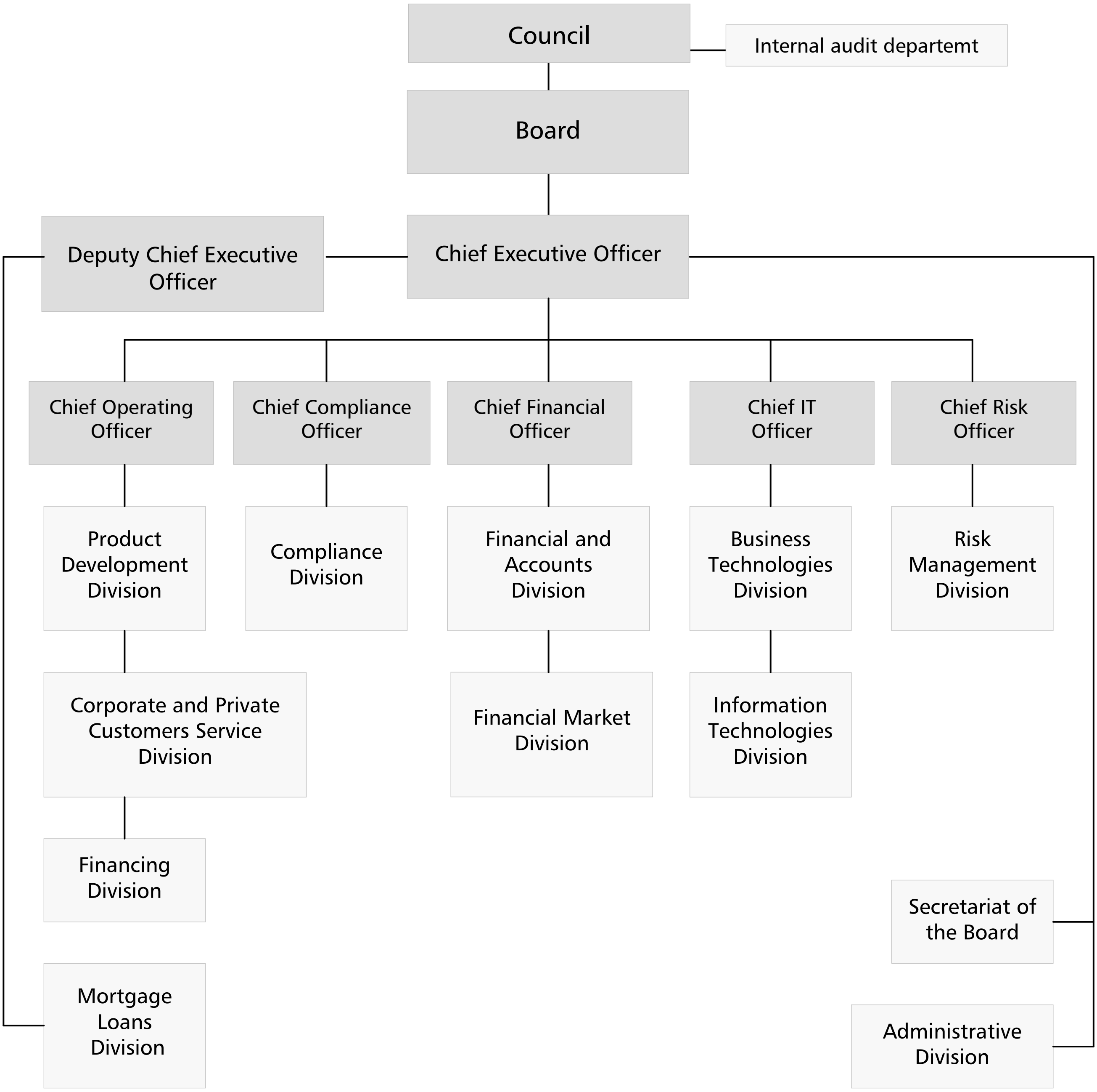
Bank's structure



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Strategy and purpose of the bank's activities

The Bank's main scope of activity is investment services, settlement products, and asset management. The business model aimed at supplying individual services to affluent and wealthy individuals and their businesses pursued by the Bank has proven to be a successful.

The Bank operates in accordance with the laws of the Republic of Latvia and the licence issued by the Bank of Latvia, which allows the Bank to provide all financial services specified in the Law on Credit Institutions.

Mission

Our mission is to become the leading independent private bank in the Eastern Europe, combining all banking services, including asset management and advisory services, in a single customer-tailored offer.

Bank's values What's More Important to us than Profit?

Ethics

The banking industry is a part of our lives. Our business standards are exactly the same as in other spheres of human activity: to speak openly with our clients, employees, and with society; to keep our promises; and not to take part in morally or legally shady deals.

Customer satisfaction

The banking industry is a service industry. The services offered can't happen in the absence of clients who use them. Banking business won't be successful if clients aren't satisfied with the service quality. To satisfy our customers, we need to surpass their expectations, and offer service better than they supposed to get. To satisfy our customers:
- provide only those services that are best meeting the customers' individual demands. To find out their individual demands, it is necessary to engage in a dialogue with the customer and adopt flexible and positive attitude to the customer, to be competent and proficient in providing services, so that total of these efforts encourages the customer to continue cooperation with the bank;
- we need to exceed their hopes, i.e. to provide service that is of higher quality than they expect.

Risk management

Banking is a high-risk business. To make a profit we need to manage risks effectively. Risks reduction requires their thorough and prudent estimation. One cannot work with what one doesn't understand. At our bank we have a system.

Independence

The Bank is proud of its status of an independent private bank. This provides us with the opportunity to work effectively, making efficient decisions and assuming full responsibility for them. This contributes to eliminating conflicts of interest probable if the bank is a part of a group of companies.

Risk management

Risks are inherent in the Group's and Bank's business and risk management is one of the Group's and Bank's strategic values, which is based on the confidence that efficient risk management is critical for the success of the Group and the Bank. Managing risks permits keeping the Group's and Bank's exposure at a level meeting their willingness and ability to undertake risks.

In the ordinary course of business, the Group and the Bank are exposed to various risks, the most significant of them being credit risk, liquidity risk, and market risks (including interest rate risk, currency risk), as well as operational risk.
Risk management stands for identification, assessment and control of potential risks.

The risk management process includes the following:
- identification, assessment and measurement of significant risks;
- setting restrictions and limits defining the maximum permissible exposure;
- regular monitoring of the compliance with the risk management policies and procedures and with any limits set;
- defining the risk assessment procedures and limits before commencing new transactions;
- quantitative risk assessment for the Group and the Bank;
- regular revision and enhancement of the policies and instructions following the market changes.

For the purpose of managing risks, risk management policies have been developed and approved by the Council. The introduction and efficiency of such policies are controlled by the Board and the Chief Risk Officer, while the practical implementation is provided by the respective business structural units, including the Risk Management Division whose functions are strictly segregated from the business functions.

To create a highly disciplined, conservative, and constructive risk management and control environment, training seminars for the staff are organised on a regular basis.
The goal of the risk management policies is to ensure efficient risk management, identify and analyse the risks inherent in the Group's and Bank's business, set relevant limits, introduce reliable control procedures, as well as control risk and exposure compliance with the applicable limits using administrative and IT resources.

The risk management system has been constantly improved following the Group's and Bank's operational and financial market development; the improvement process is controlled by the Internal Audit Department on a regular basis.

a) Credit risk

Credit risk is exposure to potential losses in case the Group's or Bank's counterparty or debtor will be unable to pay the contractual obligations to the Group or the Bank.

Credit risk management framework

Credit risk is managed according to the credit policy. Before entering into any cooperation with the customers, the Group and the Bank perform a comprehensive review of the customer's solvency and collateral.
To assess solvency of private individuals, the Bank has developed an internal rating system whereby customers are divided in categories on the basis of their income level and quality of their credit histories.

The Group and the Bank assess creditworthiness of corporate customers by conducting the financial due diligence for each new customer; subsequently, the borrower's financial position is reviewed on an annual basis. Corporate customers are granted risk/ monitoring factors, and any instances of non-compliance with these factors indicate that credit risk might have increased before the financial position of such customer is reviewed.

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Collateral is appraised by an independent appraiser accepted by the Group and the Bank. The Bank may adjust (reduce) the value defined by the independent appraiser if, in the Bank's opinion, the appraiser has not considered certain risk factors. For the purposes of loan collateral, the Bank considers such reduced value. As collateral, the Bank may accept real estate, new and used vehicles, commercial vehicles, goods held at customs or customer's warehouse, securities, technological equipment and machinery, receivables as an aggregation of property, factoring receivables, etc. Based on the collateral type and liquidity, the Group and the Bank apply the maximum acceptable proportion of the loan to be issued.

For effective credit risk management, the Bank has set up the permanent Assets Evaluation Committee which performs a regular analysis of assets and memorandum items, i.e., their recoverability. Depending on the results of such analysis, the amount of the allowance for credit losses (impairment) is determined. For the purposes of such analysis, both specific and collective (portfolio) risks are considered.

The Bank analyses the quality of the loan portfolio on a regular basis. The age of past due loans is used as one of the quality criteria. The criteria applied to corporate loans also include the borrower's business performance and prospects, its existing and forecasted cash flows to meet the liabilities, compliance with the monitoring/ risk factors set, collateral value, etc.

The Group and the Bank believe that their exposure to credit risk arises mainly from loans, investments in fixed income securities, and balances due from credit institutions.
Before entering into any cooperation with financial institutions, the Bank assesses each potential counterparty, analysing both its financial performance and other criteria, and further reviews these indicators on a regular basis.

The maximum exposure to credit risk is assessed without taking into account collateral and other credit enhancements, while the minimum exposure is assessed taking into account the fair value of the collateral at the reporting date.

The maximum exposure of the Group's and Bank's assets and memorandum items is shown in the credit risk concentration analysis. Regular stress tests of the Bank's loan portfolio are performed to assess the credit risk exposure and identify potential critical situations.

Credit risk concentration

The Group and the Bank place limits on the amount of risk for individual borrowers, and for geographical and industry concentrations as well as exposures having only one type of collateral, etc.
The exposure to any single borrower, including banks and brokers, is further restricted by sub-limits.

The issuers incorporated in a country only for the purpose of attraction of funds are disclosed as attributable to the country or region where the guarantors of the issue are located. The credit risk inherent in the Group's and Bank's securities portfolios is reflected by the credit rating granted to respective securities and issuers.

The credit risk concentration is analysed also by estimating the credit exposure ratio to equity. According to the Law on Credit Institutions, the Group and the Bank treat as high the credit exposure exceeding 10% of equity. Pursuant to the statutory requirements, the total credit exposure cannot be more than eight times as large as equity.

As at 31 December 2010 and 2009, the Group and the Bank were in compliance with this requirement. Ten major exposures as at 31 December 2010 amounted to 14.2% (7.4%) of the total Group's and Bank's gross loan portfolio.

In the event that any loan category is affected by economic factors deteriorating the condition of all loans belonging to this category, it is decided to place certain restrictions on lending in the specific industry, and potential credit losses are identified.

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The most significant part of the Bank's loan portfolio affected by economic processes in the country is the real estate development project portfolio. The Group and the Bank review this part of the loan portfolio on a regular basis. Low activity was still observed on the real estate market in 2010, which affected customer financing in this sector. No financing options for new real estate development projects are being considered at present.

The Group's and Bank's securities portfolios by the credit rating classes:

	Group/Bank					Group/Bank		
	31/12/2010					31/12/2009		
Credit ratings	At fair value LVL`000	Liquidity portfolio LVL`000	Investments held for undefined period portfolio LVL`000	Held-to-maturity LVL`000	Loans and receivables LVL`000	At fair value LVL`000	Liquidity portfolio LVL`000	Investments held for undefined period portfolio LVL`000
AAA to AA-	19,362	106,985	2,840	111,604	-	-	48,710	2,146
A+ to A-	-	-	-	164	-	-	-	-
BBB+ to BBB-	-	-	20,590	27,484	606	-	-	16,860
BB+ to BB-	-	-	18,447	6,795	3,652	-	1,985	12,283
B+ to B-	5	-	16,325	9,003	4,451	-	-	16,399
Below B-	-	-	784	62	2,133	12	-	2,081
No rating	-	-	460	-	219	-	-	1,912
Shares and investments in funds	674	-	2,226	-	-	52	-	2,147
Securities portfolio, net	**20,041**	**106,985**	**61,672**	**155,112**	**11,061**	**64**	**50,695**	**53,828**

b) Liquidity risk

Liquidity is the Group's and Bank's ability to maintain or ensure sufficient cash and cash equivalents to meet the expected (everyday) or sudden (critical) legally justified claims of its creditors. This means the Group's and Bank's ability to turn their assets into cash with minimal loss or ensure reasonably priced credit facilities.

The Chief Risk Officer (CRO) is responsible for liquidity risk management. The Risk Management Division is responsible for liquidity risk evaluation and control. The Chief Financial Officer (CFO) is responsible for liquidity management and the Financial Market Division is responsible for ensuring the required liquidity level and compliance with the set limits according to the policies and instructions adopted.

The key principles and procedures to timely identify, analyse and control liquidity risk are laid down in the liquidity management policy.

For ordinary liquidity risk management purposes, the Bank applies the following indicators having certain limits and restrictions set:

- deposit coverage ratio;
- net liquidity positions by all currencies in total and by each separate currency;
- current liquidity ratio;
- major deposits on demand ratio to liquid assets on demand;
- sum of term deposits of one customer (group of related customers).

To timely identify the potential deterioration in the liquidity position, an early warning indicators system has been designed:

- substantial daily reduction of the amounts to be claimed under savings accounts and term deposits with the remaining maturities of "Less than 30 days";
- simultaneous decrease of the weighted average duration and the total balance of term deposits;
- substantial growth of deposits claimed before their contractual maturity;
- decrease of the proportion of liquid assets in the total assets of the Bank;
- negative information reported in the mass media about the Bank or its related parties that may harm the Bank's reputation;
- the increasingly reported instances of limits reduced or annulled by counterparties.

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Contingency liquidity risk

Contingency liquidity risk relates to the organisation and planning for liquidity management in times of stress. Within the Bank a specific crisis team is responsible for the liquidity management in times of crisis. This crisis team consists of the CEO, CRO, CFO, the Financial Market Division and the Risk Management Division. The Group and the Bank have defined principles to identify liquidity crisis stages and actions to overcome crisis situations. The main objective of Bank's contingency plans is to enable senior management to act effectively and efficiently at times of crisis. The contingency plans are established for addressing temporary and long-term liquidity disruptions caused by a general event in the market or a Bank specific event. These plans ensure that all roles and responsibilities are clearly defined and the necessary management information is in place.

According to the internal classification of the Group and the Bank, several liquidity crisis stages are distinguished: potential liquidity crisis, short-term and long-term liquidity crisis. Each stage has quantitative and qualitative indicators fixed which, if observed, also require certain actions to enhance liquidity. The Bank performs regular liquidity stress tests to identify the sources of potential liquidity problems, determine when the mandatory ratios may be breached or the crisis indicators listed in the Liquidity Crisis Manual may emerge as well as establish whether the Bank's liquidity management documents need to be revised.

The management of the Group and the Bank continued to focus specifically on liquidity issues. Owing to the adequate liquidity risk management policy and internal control and communication system, the Bank managed to ensure and maintain high liquidity ratio - as at 31 December 2010, the liquidity ratio reached 68.10% (56.15%). The FCMC stipulates that the Bank should maintain the sufficient amount of liquid assets to meet its contractual liabilities, but no less than 30% of the Bank's total current liabilities.

Liquidity ratios of the Group and the Bank:

	Group/ Bank			Group/ Bank		
	2010			2009		
Liquidity ratio	Highest	Lowest	Average	Highest	Lowest	Average
	%	%	%	%	%	%
on demand	46.6	32.2	38.4	40.2	26.2	32.5
less than 30 days (as required by the FCMC)	71.0	59.1	64.4	57.5	33.8	43.2
less than 90 days	70.2	58.3	64.3	53.1	39.8	45.0

c) Market risk

The exposure of the trade portfolio to market risk and the capital charge for market risk is determined according to the standard approach described in the Regulations for Calculation of Minimum Capital Requirement whereby the positions for general risk debt securities are calculated under term the method.

d) Currency risk

The Group and the Bank are exposed to negative effects of fluctuations in the foreign currency exchange rates on their financial position and cash flows. The exposure to currency risk is calculated for each separate currency and includes assets and liabilities denominated in foreign currencies, as well as cash flows arising from derivatives. The Bank has major open positions in EUR (euros) and USD (US dollars). Considering that the lat is pegged to the euro, the currency risk related to the Bank's open position in EUR is minimal. The Bank's open currency position in USD is also rather small as it is hedged by using currency forwards/ futures. As at 31 December 2010, the Bank's open currency position in USD was 0.1% (5.2%) of Bank's equity and, therefore, the effect of changes in the USD exchange rate is insignificant, and the Bank does not conduct more detailed sensitivity analysis, only controlling this risk by applying the limits specified in the Limits Policy. As at 31 December 2010, all the above limits had been met.

The Bank's Limits Policy defines major principles for limits application and control; limits for open foreign currency positions stipulate restrictions for each separate currency open position and total open position that are controlled on a daily basis.

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The Law on Credit Institutions requires that Bank's open positions in each foreign currency may not exceed 10% of equity and that the total Bank's foreign currency open position may not exceed 20% of equity.
As at 31 December 2010, the Bank was in compliance with the above requirements of the Law on Credit Institutions.

e) Interest rate risk

Interest rate risk represents the adverse effect of the market interest rate fluctuations on the Bank's financial performance. The Risk Management Division ensures interest rate risk assessment and management for both trading and non-trading portfolios. The Financial Market Division is responsible for maintaining interest rate risk within specified limits.

Assessment of interest rate risk is conducted striving to cover all risk elements – repricing risk, yield curve risk, basis risk, and option risk.
Interest rate risk is assessed both in terms of income and economic value. The term *economic value* means the shareholders' equity's economic value that is the difference between the economic value of assets and that of liabilities. For the purposes of assessment of extraordinary circumstances, stress tests are applied.

For the purposes of hedging interest rate risk, the limits of acceptable reduction in economic value and modified duration of the investments' held for undefined period portfolio are fixed. Derivative financial instruments are utilised to hedge interest rate risk.

The assets, liabilities and memorandum items distribution into maturity bands follows such principles:
- financial instruments with a fixed interest rate are presented by the earlier of the repayment/settlement/maturity date;
- financial instruments with a variable interest rate are presented according to next contractual repricing date or interest rate repricing date.

Derivatives are represented in two entries: the first entry describes the notional amount of the underlying assets, whereas the other one is a compensatory entry showing the opposite value.

The effect of interest rate risk on the economic value is calculated according to the duration method, i.e., the parallel increase in interest rates by 1 per cent (or 100 basis points), while the effect on profit/loss is analysed applying the gap analysis, i.e. analysing the maturity gaps of interest rate sensitive assets and liabilities and aggregating the effect calculated (profit or loss) for each maturity band up to one year.

The Bank performs regular interest rate stress tests aimed at assessing the effect of adverse changes in interest rates on the Bank's income and economic value in the event of a tough market situation.

The following table presents the Group's and Bank's sensitivity to changes in interest rates and the effect of such changes on equity and profit in 2010 and 2009:

		Group/ Bank 31/12/2010		**Group/ Bank 31/12/2009**	
		+100bps	-100bps	+100bps	-100bps
		LVL'000	**LVL'000**	**LVL'000**	**LVL'000**
Total for all currencies	Effect of changes on equity	(1,313)	1,313	(1,337)	1,337
	Effect of changes on profit/ loss	3,788	(3,788)	(1,392)	1,392
USD	Effect of changes on equity	(1,313)	1,313	(1,261)	1,261
	Effect of changes on profit/ loss	695	(695)	(2,393)	2,393
EUR	Effect of changes on equity	-	-	(76)	76
	Effect of changes on profit/ loss	2,522	(2,522)	765	(765)
LVL	Effect of changes on equity	-	-	-	-
	Effect of changes on profit/ loss	572	(572)	236	(236)

Non-financial risks

During the course of their operations, the Group and the Bank encounter also non-financial risks (including operational risk, reputational risk, etc.) with exposure to sudden loss. The cause of such risks may be, for instance, clerical errors or fraud, break-downs in information systems, insufficient internal control and procedures, etc. The Bank makes every effort to maintain the lowest possible risk level, meanwhile striving at not exceeding a reasonable level of expense. Internal control within the Bank's structural units and the control exercised by the Risk Management Division are one of the measures taken to prevent the potential loss.

f) Operational risk

Operational risk is a risk of direct or indirect loss caused by non-complying or incomplete internal processes, human error or systems failure, as well as external factors. Operational risk comprises legal risk but excludes strategic and reputational risk.

Operational risk is inherent in all products, activities, processes, and systems of the Group and the Bank.

The operational risk management policy is approved by the Council of the Bank. The Board of the Bank is responsible for considering the risk analysis results and setting limits and other qualitative and quantitative indicators based on such results, so defining the level of operational risk acceptable for the Group and the Bank. The Chief Risk Officer (CRO) is responsible for monitoring the operational risk management process and making related final decisions within the limits fixed in the policy. The Risk Management Division is responsible for the centralisation and coordination of the operational risk management.

Given that businesses and processes for which operational risk is being assessed are different and specific, each risk event management is a responsibility of the head of a respective structural unit, according to the relevant internal regulations.

The key principles allowing efficient operational risk management are as follows:
- setting up an adequate operational risk management system;
- employing an adequate method to identify and assess operational risk;
- monitoring operational risk on a regular basis;
- controlling and/ or mitigating operational risk adequately;
- ensuring business continuity.

To manage the Group's and Bank's exposure to operational risk, in September 2008 an operational risk event database was established. The key objectives of the database are as follows:
- collection of data about operational risk events and losses of the Group and the Bank;
- analysis of operational risk events and losses;
- assessment of the frequency of operational risk events and significance of operational risk losses;
- prevention of potential losses, based on the event assessment;
- definition of the major tendencies and making forecasts of future operational risk losses.

Information is registered and categorised in the database following the good practice principles defined by the Operational Riskdata eXchange Association (ORX). In addition to events resulting in actual losses, information about events for which no actual losses have been registered is also aggregated in the database, which enables the Bank to identify potential losses and take all required measures to prevent such losses.

During the reporting year, approximately 1,499 (1,300) events were registered in the database, of which only 82 (85) events were those which resulted in actual losses amounting to LVL 32,8 (23,4) thousand. The considerable number of the identified and registered events and, at the same time, rather a small amount of loss testify to the active involvement of the Group's and Bank's employees in the operational risk management and to the effectiveness of the control environment.

g) Reputation risk

Reputation risk is non-quantifiable risk. The impact and losses related to this risk are hard to determine. The reputation risk management (assessment, applicable techniques, control) in the Bank is specified in the

Reputation Risk Management Policy. The Bank is planning to summarise information on the respective risk factors and develop the methodology for the quantification of compliance and reputations risks. It should also be noted that reputation risk is closely related to operational risk (incl. legal risk), therefore it is sometimes difficult to separate them. Therefore, so far the Bank has resolved not to allocate and define the necessary funds for covering the above mentioned risk.

h) IS risk

The Bank has developed Information Technology Security Policy, Regulations for Information System Risk Analysis, Security Requirements for Information Systems under Development, and other regulative acts ensuring information system risk management. According to the Operational Risk Management Policy adopted by the Bank, information system risk is included in operational risk, therefore for the purpose of capital adequacy assessment it was resolved not to separate it from operational risk capital requirement. The Bank will analyze the data compiled in the Operational Risk Event and Loss Database to determine the possibility and necessity of defining a separate capital requirement for information system risk.

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Income statements

	2010 (audited)		2009 (audited)	
	Group	Bank	Group	Bank
	LVL '000	LVL '000	LVL '000	LVL '000
Interest income	36,431	36,375	40,118	40,909
Interest expense	(18,850)	(18,808)	(22,321)	(22,466)
Income from dividends	4	52	62	261
Commission and fee income	22,876	20,146	16,072	14,901
Commission and fee expense	(3,241)	(2,979)	(2,867)	(2,696)
Net gain/ (loss) from financial assets and liabilities at fair value through profit or loss	12,589	12,589	(1,539)	(1,539)
Net realised gain/ (loss) from available-for-sale financial assets	418	418	363	363
Net realised (loss)/ gain from financial assets at amortised cost	(1,823)	(1,823)	528	528
Net result from foreign exchange trading and revaluation	(1,153)	(1,209)	8,424	8,496
Gain/ (loss) from sale of tangible and intangible fixed assets	270	(10)	(204)	(204)
Other income	1,873	1,457	2,129	628
Other expense	(1,672)	(2,499)	(1,971)	(1,595)
Administrative expense	(22,494)	(20,186)	(20,641)	(18,597)
Depreciation	(1,692)	(1,587)	(1,815)	(1,725)
Change in allowances for credit losses	(28,917)	(28,917)	(36,859)	(36,859)
Impairment expenses	(2,881)	(846)	(5,189)	(3,157)
Corporate income tax	703	880	3,541	3,532
Net loss for the year	**(7,559)**	**(6,947)**	**(22,169)**	**(19,220)**
Attributable to:				
Equity holders of the Bank	(7,519)		(21,358)	
Non-controlling interests	(40)		(811)	

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Balance sheet

	At 31 december 2010 (audited)		At 31 december 2009 (audited)	
	Group	Bank	Group	Bank
Assets	LVL '000	LVL '000	LVL '000	LVL '000
Cash and demand deposits with central banks	82,120	82,120	44,986	44,986
Balances due from credit institutions	325,352	325,326	203,569	203,537
Financial assets at fair value through profit or loss	23,372	23,372	9,499	9,499
Available-for-sale financial assets	168,657	168,657	104,523	104,523
Loans and receivables	528,872	528,561	550,580	553,475
Loans	517,811	517,500	531,444	534,339
Debt securities and other fixed income securities	11,061	11,061	19,136	19,136
Held to maturity	155,112	155,112	-	-
Prepaid expense and accrued income	339	292	505	451
Tangible fixed assets	7,954	5,253	6,077	5,747
Investment properties	20,658	16,670	20,371	16,622
Intangible fixed assets	3,701	3,548	3,491	3,337
Investments in subsidiaries	-	58,661	-	36,066
Current corporate income tax receivables	266	176	2,024	1,936
Deferred income tax	5,736	5,718	5,458	5,079
Other assets	45,388	5,099	26,644	6,871
Total assets	**1,367,527**	**1,378,565**	**977,727**	**992,129**
Liabilities				
Demand deposits from credit institutions	1,906	1,906	1,027	1,027
Financial liabilities at fair value through profit or loss	226	226	176	176
Financial liabilities at amortised cost	1,264,255	1,272,702	887,172	897,686
Term deposits from credit institutions	3,502	550	4,929	1,958
Deposits	1,236,791	1,248,190	858,503	869,017
Subordinated deposits	23,962	23,962	28,669	28,669
Securities issued	22,921	22,921	12,995	12,995
Deferred income and accrued expense	2,769	2,460	1,816	1,749
Current corporate income tax liabilities	150	-	15	-
Deferred income tax	21	-	22	-
Other liabilities	4,328	2,973	589	2,456
Total liabilities	**1,296,576**	**1,303,188**	**903,812**	**916,089**
Total shareholder's equity	70,951	75,377	68,986	74,082
Total liabilities and shareholder's equity	**1,367,527**	**1,378,565**	**972,798**	**990,171**
Memorandum items				
Contingent liabilities	21,125	21,125	16,884	16,884
Financial commitments	12,934	12,934	10,210	10,210

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Performance indicators

Title of the entry	2010 (audited)	2009 (audited)
Return on equity (ROE) (%)	-8.99	-24.44
Return on assets (ROA) (%)	-0.55	-1.91