AS “Akciju komercbanka “Baltikums”” non-audited Consolidated Financial Statement as of 30 June, 2008

Contents

Management Report

26 August 2008

In the first six months of 2008, performance indicators of JSC Akciju komercbanka Baltikums (hereinafter referred to as the Bank, Komercbanka Baltikums) continued to grow and the Bank consolidated its position in the selected segment.

Komercbanka Baltikums continued to develop in accordance with its strategy whose major emphasis was to offer a dynamic, modern and, what is most important, exclusive service for its customers.

Similarly to the previous years, the Bank worked along two clearly defined directions: trade and shipping finance, as well as financial markets products and wealth management. In the first half of 2008, the Bank was focusing on meeting the needs of its current and potential customers, introducing private banking services, which are in a growing demand nowadays, and working to extend the range of such products. As a result, the Bank was able to offer several new opportunities to its customers interested in those investment and savings products.

In the first six months, the Bank's profit amounted to LVL 2.135 million, thus far exceeding estimates made earlier in the year. The Bank's assets have reached LVL 126.530 million (a rise of 28% since the beginning of the year). By late June, Komercbanka Baltikums had increased its deposit base by 27% since the beginning of this year, and the amount of deposits had reached LVL 91.679 million.

Komercbanka Baltikums's loan portfolio has risen to LVL 31.208 million. Similarly to 2007, most of the loans were issued for projects related to shipping and international trade finance.

Increasing the equity base (up to LVL 15.178 million), raising funds by issuing notes (to the total amount of EUR 15 million) as well as rising customer deposits allow the Bank to boost the loan portfolio and strengthen its position in the preferred market niche.

In the first half of 2008, the Bank continued to optimise its customer base. Related companies operating in Russia, Ukraine and Kazakhstan substantially contributed to the Group's business by attracting new customers. Despite such a considerable rise in the number of customers, the Bank closely monitors customer operations by implementing the principles "Know Your Customer" and "Know Your Customer's Business".

In the first six months of 2008, Komercbanka Baltikums opened its representative office in Almaty (Kazakhstan). It was the first representative office in the international network established by the Bank. Extending such a network of international regional branches and representative offices is one of the Bank's strategic tasks. Komercbanka Baltikums believes that Central Asia has a huge development potential. Latvia and Kazakhstan enhance their business contacts continuously and develop transactions in the area of transit business. In the nearest future Komercbanka Baltikums plans to establish a substantial network of representative offices to provide information on the Bank's services for its potential customers. Currently, the relevant registration documents have been filed with the aim to open a representative office in Kiev (Ukraine).

Komercbanka Baltikums has extended the network of its correspondent banks for transfers in euros (EUR) and Kazakh tenge (KZT) in order to save customers' time and funds. The Bank opened correspondent accounts with KBC Bank NV (Brussels, Belgium) and BTA Bank JSC (Almaty, Kazakhstan).

We consider it a major achievement that Deutsche Bank has positively evaluated the processing quality of Komercbanka Baltikums' s outgoing payments and awarded the Bank an annual Deutsche Bank's 2007 EUR Straight-Through Processing Excellence Award. The award certifies the professionalism of the Bank's officers and the quality of the Bank's technologies ensuring the high quality of the payment-execution process.

This year, the process of optimisation of Baltikums Holding structure continued, where Komercbanka Baltikums was assigned a central place. Shareholders of JSC Baltikums Apdrosinasanas Grupa and JSC Baltikums Bankas Grupa wish to restructure Baltikums Holding by consolidating financial and insurance companies into AS Baltikums Bankas Grupa.

In the first half of 2008, the Bank has acquired a subsidiary - SIA Konsalting Invest. Its line of business is financial consulting and real estate management.

The Bank has also signed two agreements on sale of its subsidiaries. Komercbanka Baltikums signed an agreement with JSC Latvijas Krajbanka on the sale of 93.46% shares of AAS Baltikums Dziviba. The transaction's rationale is based on the fact that the Bank is closely following its strategy of refraining from the involvement in retail banking operations.

Also, Komercbanka Baltikums has signed an agreement with Invalda AB (Lithuania) on the purchase of 100% shares of IPS Finasta Asset Management (investment management company registered in Latvia) and on the sale of 100% shares of IPAS Baltikums Asset Management (investment management company registered in Latvia) to Invalda AB.

The above transactions will be finalised following the approval by supervisory authorities as well as after completing other necessary steps.

We are grateful to all our clients for their co-operation and trust and express deep confidence in the continuing success of our mutually beneficial business relations.

Aldis Reims,
JSC Akciju komercbanka Baltikums
Chairman of the Board

Consolidated Income Statement

	30.06.2008 LVL'000	30.06.2007 LVL'000	30.06.2008 EUR'000	30.06.2007 EUR'000
Interest income	2 254	2 347	3 207	3 339
Interest expense	-731	-821	-1 040	-1 168
Fees and commission income	2 020	1 260	2 874	1 793
Fees and commission expense	-387	-266	-551	-379
Net profit/loss from financial assets and liabilities valued at fair value	230	89	327	127
Net trading income from foreign exchange	1 607	37	2 287	53
Trading income from financial instruments and foreign exchange	0	139	0	198
Other operating income	114	49	162	70
Administrative expenses	-1 804	-1 245	-2 567	-1 771
Depreciation and amortization	-98	-40	-139	-57
Other operating expenses	-275	-66	-391	-94
Provisions for impairment losses	-408	-82	-581	-117
Income from decrease of provisions	0	8	0	11
Income before corporate income tax	2 522	1 409	3 588	2 005
Income tax	-387	-202	-550	-288
Profit for the period	**2 135**	**1 207**	**3 038**	**1 717**
Attributable to:				
Equity holders of the Bank	*2 135*	*1 207*	*3 038*	*1 717*
Net income	**2 135**	**1 207**	**3 038**	**1 717**

The fixed exchange rate of the Bank of Latvia is 1 EUR=0.702804 LVL

Consolidated Balance Sheet

Position	30.06.2008 LVL'000	30.06.2007 LVL'000	30.06.2008 EUR'000	30.06.2007 EUR'000
Cash and deposits with the Bank of Latvia	11 753	5 020	16 723	7 143
Due from credit institutions on demand	41 837	42 497	59 529	60 468
Trading assets	**22 055**	**14 128**	**31 381**	**20 102**
Financial assets at fair value through profit or loss	0	246	0	350
Available-for-sale financial assets	10	1 845	14	2 625
Loans and receivables	31 208	22 526	44 405	32 052
Held to maturity financial investments	0	0	0	0
Investments in associated entities and in subsidiaries	3 072	3 071	4 371	4 370
Intangible assets	226	195	322	277
Property, Plant and Equipment	1 651	170	2 349	242
Investment property	3 220	565	4 582	803
Other assets	11 471	325	16 322	462
Prepayments and accrued income	27	156	38	222
Total assets	**126 530**	**90 744**	**180 036**	**129 116**
Balances due to credit institutions on demand	2 841	1 200	4 042	1 707
Trading liabilities	102	0	145	0
Financial liabilities carried at amortized cost	**103 919**	**76 246**	**147 863**	**108 488**
Balances due to credit institutions on term	*1 608*	*300*	*2 288*	*427*
Customers deposits	*91 679*	*65 380*	*130 447*	*93 027*
Notes payable	*10 632*	*10 566*	*15 128*	*15 034*
Insurance contracts	0	760	0	1 081
Tax liabilities	98	109	141	154
Other liabilities	1 843	154	2 622	220
Total liabilities	**108 803**	**78 469**	**154 813**	**111 650**
Shareholders' equity				
Share capital	15 178	10 525	21 596	14 976
Reserve capital and other reserves	17	17	24	24
Retained earnings	397	352	565	501
Profit of the year	2 135	1 207	3 038	1 717
Attributable to:				
Equity holders of the Bank	*2 135*	*1 207*	*3 038*	*1 717*
Minority interest	0	174	0	248
Total liabilities and shareholders' equity	**126 530**	**90 744**	**180 036**	**129 116**
Contingent liabilities	0	3	0	4

Financial commitments	4 306	6 881	6 127	9 791
Assets / Liabilities under management	**3 675**	**1 335**	**5 229**	**1 900**

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Consolidated Statement of Changes in Shareholders Equity

	Share capital, LVL'000	Reserve capital and other reserves, LVL'000	Retained earnings, LVL'000	Profit for the year, LVL'000	Minority interest, LVL'000	Total, LVL'000
Balance as at 31 December 2006	**7 450**	**17**	**1 484**	**8 951**	**174**	**9 125**
Profit for the year	0	0	2 009	2 009	8	2 017
Issue of shares	3 075	-	-	3 075	-	3 075
Dividends paid	0	0	-1 132	-1 132	0	-1 132
Balance as at 31 December 2006	**10 525**	**17**	**2 361**	**12 903**	**182**	**13 085**
Profit for the year	0	0	2 135	2 135	0	2 135
Issue of shares	4 653	0	0	4 653	0	4 653
Sale of subsidiaries	0	0	0	0	-182	-182
Dividends paid	-	0	-1 964	-1 964	-	-1 964
Balance as at 30 June 2008	**15 178**	**17**	**2 532**	**17 727**	**0**	**17 727**

	Share capital, EUR'000	Reserve capital and other reserves, EUR'000	Retained earnings, EUR'000	Profit for the year, EUR'000	Minority interest, EUR'000	Total, EUR'000
Balance as at 31 December 2006	**10 600**	**24**	**2 112**	**12 736**	**248**	**12 984**
Profit for the year	0	0	2 859	2 859	11	2 870
Issue of shares	4 375	0	0	4 375	0	4 375
Dividends paid	-	-	-1 611	-1 611	-	-1 611
Balance as at 31 December 2007	**14 975**	**24**	**3 360**	**18 359**	**259**	**18 618**
Profit for the year	0	0	3 038	3 038	0	3 038
Issue of shares	6 621	0	0	6 621	0	6 621
Sale of subsidiaries	0	0	0	0	-259	-259
Dividends paid	-	-	-2 795	-2 795	-	-2 795
Balance as at 30 June 2008	**21 596**	**24**	**3 603**	**25 223**	**0**	**25 223**

The fixed exchange rate of the Bank of Latvia is 1 EUR=0.702804 LVL

Consolidated Cash Flows Statement

	30.06.2008 LVL'000	30.06.2007 LVL'000	30.06.2008 EUR'000	30.06.2007 EUR'000
Cash flow from operating activities				
Profit before income tax	2 517	1 409	3 581	2 005
Depreciation and amortization	69	40	98	57
Impairment of financial assets, net	408	81	581	115
Unrealized loss from foreign exchange	109	116	155	165
Investment property and other revaluation	39	-192	55	-273
Profit from the sale of subsidiaries	255	-1	363	-1
Increase in cash and cash equivalents from operating activities before changes in assets and liabilities	**3 397**	**1 453**	**4 833**	**2 068**
Changes in loans and receivables	-5 688	-4 732	-8 093	-6 733
Changes in financial assets classified as available–for-sale	0	69	0	98
Changes in financial assets classified as trading assets	-8 934	-4 079	-12 712	-5 804
Changes in financial assets classified at fair value through profit or loss	15	-10	21	-14
Changes in financial assets classified as held-to-maturity financial assets	-362	-513	-515	-730
Changes in prepayments and accrued income	2	-17	3	-24
Changes in other assets	-11 121	41	-15 824	58
Changes in other customer deposits	19 537	27 477	27 799	39 096
Changes in financial liabilities held for trading	-86	0	-122	0
Changes in other and tax liabilities	-92	-66	-131	-94
Changes in deferred income and accrued expense	185	-61	263	-87
Net cash from operating activities before income tax	**-3 147**	**19 562**	**-4 478**	**27 834**
Income taxes paid	-488	-220	-693	-312
Increase in cash and cash equivalents from operating activities	**-3 635**	**19 342**	**-5 171**	**27 522**
Cash flow from investing activities				
Acquisition of fixed and intangible assets	-1 496	-100	-2 129	-142
Proceeds from disposals of fixed and intangible assets	120	3	171	4
Cash flow from other investing	-503	122	-716	174

activities				
Acquisition of investments in subsidiaries, net of cash acquired	-1 422	-3 071	-2 023	-4 370
Net value of subsidiaries sale	1 989	232	2 830	330
Cash and cash equivalents used in investing activities	**-1 312**	**-2 814**	**-1 867**	**-4 004**
Cash flow from financing activities				
Issue of shares	4 653	3 075	6 621	4 375
Proceeds from issue of debt securities	0	7 106	0	10 111
Dividends paid	-1 964	-1 132	-2 795	-1 611
Cash and cash equivalents provided by financing activities	**2 689**	**9 049**	**3 826**	**12 875**
Net increase in cash and cash equivalents	**-2 258**	**25 577**	**-3 212**	**36 393**
Cash and cash equivalents at the beginning of the year	51 938	21 020	73 902	29 909
Loss from foreign exchange revaluation	-109	-116	-155	-165
Cash and cash equivalents at the end of the year	***49 571***	***46 481***	***70 535***	***66 137***

The fixed exchange rate of the Bank of Latvia is 1 EUR=0.702804 LVL

Notes

1. GENERAL INFORMATION

The Bank was established on 22nd June 2001, when it was incorporated in the Republic of Latvia as a joint stock company. The address of the Bank is Maza Pils iela 13, Riga, LV-1050. The Bank is a commercial bank specialising in the servicing of export and import operations, trade finance and investment management. The Bank operates in accordance with Latvian legislation and the licence issued by the Bank of Latvia.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(1) Statement of compliance

The Bank's financial statements have been prepared in compliance with the EU-endorsed International Financial Standards (IFS) and the Permanent Interpretation Committee's interpretations as well as the Financial and Capital Market Commission's regulations that were in effect at the time of the preparation of the financial statements.

(2) Basis for preparation of the financial statements

The Bank maintains its accounting records in accordance with the legislation of the Republic of Latvia. The Bank's financial year corresponds to the calendar year.

The financial statements are based on the accounting records prepared in accordance with the cost accounting principle or fair value, as appropriate. The financial statements are prepared on a fair value basis for derivative financial instruments, financial assets and liabilities held for trading and available-for-sale assets except those for which a reliable measure of fair value is not available. Other financial assets and liabilities and non-financial assets and liabilities are stated at amortised cost or historical cost.

The accounting policies used in the preparation of the financial statements are consistent with those used in the financial statements for the period ending 30 June 2007.

(3) Foreign currency translation

The currency of the Republic of Latvia – lat (LVL) – is used in the financial statements. All assets and liabilities and off-balance sheet claims and liabilities in foreign currencies are revaluated in lats using the end of period exchange rates determined by the Bank of Latvia. Gains and losses arising from revaluation are included in the profit and loss statement for the period, except for differences, which arise from the revaluation of available-for-sale elements of the shareholders' equity.

The foreign currency exchange rates for the principal currencies that were used as of the end of the period were as follows:

	As of 30 June 2008	**As of 30 June 2007**
EUR	0,702804	0,702804
GBP	0,888000	1,044000
LTL	0,204000	0,204000

RUB	0,019000	0,020200
UAH	0,097700	0,104000
USD	0,447000	0,522000

Transactions in foreign currencies are revaluated in lats according to the date of the transaction using exchange rates set by the Bank of Latvia.

(4) Going concern

The consolidated and Bank's financial statements have been prepared on a going concern basis, which contemplates the realisation of assets and the satisfaction of liabilities in the normal course of business.

(5) Basis of consolidation

Consolidated financial statements as of 30 June 2007 include financial statements of the Bank and financial statements of the following companies:

Company	State of origin	Company's profile	Share of capital, %
IPAS Baltikums Asset Management	Latvia	Financial services	100.00
SIA Baltikums Lizings	Latvia	Financial services	100.00
AAS Baltikums Dziviba	Latvia	Insurance services	93.46

Consolidated financial statements as of 30 June 2008 include financial statements of the Bank and financial statements of the following companies:

Company	State of origin	Company's profile	Share of capital, %
IPAS Baltikums Asset Management	Latvia	Financial services	100.00
SIA Baltikums Lizings	Latvia	Financial services	100.00
SIA Baltikums Direct	Latvija	Lawyer services	100.00
SIA Konsalting Invest	Latvija	Financial services	100.00

Consolidated balance sheet is composed of balance sheets of all subsidiaries, which are controlled by the Group and in where Group has more than half voting rights. Control exists when the company has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. Subsidiaries are consolidated from the date on which effective control is transferred to the Group and are no longer consolidated from the date of disposal.
During consolidation all significant transactions between Group's companies are cancelled.
While consolidating subsidiaries assets and liabilities are revaluated using exchange rates of The Bank of Latvia on balance day. Incomes and losses are recalculated in Latvian lats using average for the year exchange rate on balance date.

(6) Financial instruments

a) Classification:

Financial assets and liabilities at fair value through profit and loss are those that have been designated by the Bank at inception as at fair value through profit and loss and those classified as held for trading. Trading instruments are those that the Bank principally holds for the purpose of generating a profit from short-term fluctuations in the price of the instruments.
Originated loans and receivables are loans and receivables that the Bank has created by providing funds to customers other than those created with the intent to be sold immediately or in the short-term. Originated loans and receivables include loans and advances to banks and customers other than purchased loans.
Held-to-maturity assets are financial assets with fixed or determinable payments and fixed maturity that the Bank has the intent and ability to hold to maturity. These include certain debt instruments.
Available-for-sale assets are financial assets that are not held for trading purposes, originated loans and receivables, or held to maturity.

b) Recognition

Financial instruments are recognized in the balance sheet on a settlement date basis. Originated loans and receivables are recognised on the day they are transferred to or originated by the Bank.

c) Measurement

Financial instruments are measured initially at fair value plus transaction costs if the financial instruments are not at fair value through profit and loss account.
Subsequent to initial recognition, all financial assets and liabilities at fair value through profit and loss and all available-for-sale assets are measured at fair value, except for any instrument that does not have a quoted market price in an active market and whose fair value cannot be reliably measured. These are stated at cost, including transaction costs, less impairment losses. The fair value is assessed based on quoted market prices.
All non-trading financial assets and liabilities, originated loans and receivables and held-to-maturity assets are measured at amortised cost using the effective interest rate method. All such financial instruments are subject to revaluation for impairment.

d) Fair value measurement principles

The fair value of financial instruments is based on their quoted market price at the balance sheet date without any deduction for transaction costs. If a quoted market price is not available, the fair value of the instrument is estimated using pricing models or discounted cash flow techniques.
Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate is a market related rate at the balance sheet date for an instrument with similar terms and conditions. Where pricing models are used, inputs are based on market related measures at the balance sheet date.
The fair value of derivatives that are not exchange-traded is estimated at the amount that the Bank/(Group) would receive or pay to terminate the contract at the balance sheet date taking into account current market conditions and the current creditworthiness of the counterparties.

e) Gains and losses on subsequent measurement

Gains and losses arising from a change in the fair value of all financial assets and liabilities at fair value through profit and loss are recognised in the income statement. Gains and losses arising from a change in the fair value of available-for-sale securities are recognised directly in equity. The Bank does not apply hedge accounting.

f) Derecognition

A financial asset is derecognised when the Bank loses control over contractual rights that comprise that asset. This occurs when the rights are realised, expire or are surrendered. A financial liability is derecognised when it is extinguished.
Available-for-sale assets, financial assets and liabilities at fair value through profit and loss, held-to-maturity instruments and originated loans and receivables are derecognised on the day they are transferred by the Bank.

(7) Interest income and expenses

Interest income and expense are recognised in the income statement as they accrue, taking into account the effective yield of the asset/liability or an applicable floating rate. Interest income and expense include the amortisation of any discount or premium or other differences between the initial carrying amount of an interest bearing instrument and its amount at maturity calculated on an effective interest rate basis.
Recognition of interest income is discontinued when there is uncertainty regarding the repayment of interest or principal.

(8) Fee and commission income

Fee and commission income is recognised when earned or incurred.

(9) Investments

Subsidiaries
Subsidiaries are entities in which the Group, directly or indirectly, has power to control or exercise control over financial and operating policies.
Investments in subsidiaries are carried at cost in the Bank's financial statements. The Bank recognizes income from the investment only to the extent that the Bank receives distributions from accumulated profits of the subsidiary arising after the date of acquisition. Distributions received in excess of such profits are regarded as a recovery of investment and are recognized as a reduction of the cost of the investment.

Investments in associates
Associates are those enterprises in which the Bank has significant influence, but not control, over the financial and operational policies. The consolidated financial statements include the Bank's share of the total recognized gains and losses of associates on an equity accounted basis, from the date that significant influence effectively commences until the date that significant influence effectively ceases. When the Bank's share of losses exceeds cost, the carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Bank has incurred obligations in respect of the associate.

(10) Loans

Loans and advances are classified as originated loans and receivables and carried at amortised cost, where cost is defined as the fair value of cash consideration given to originate those loans. Loans are recognized in the balance sheet at the amount of the outstanding value, less impairment for doubtful debts.

The Bank mainly grants commercial and industrial loans to customers.

(11) Impairment

The carrying amounts of the Bank's assets, other than deferred tax assets, are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the assets' recoverable amounts are estimated.

Calculation of recoverable amount

The recoverable amount of the Bank's loans and receivables is calculated as the present value of expected future cash flows, discounted at the original effective interest rate inherent in the asset. The recoverable amount of the Bank's available-for-sale investments is their fair value.

Reversals of impairment

An impairment loss in respect of loans and receivables is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised.

(12) Interest bearing borrowings

Interest-bearing borrowings are recognised initially at fair value, net of any transaction costs incurred. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings.
When borrowings are repurchased or settled before maturity, any difference between the amount repaid and the carrying amount is recognised immediately in the income statement.

(13) Depreciation and amortisation of fixed and intangible assets

Fixed assets and intangible assets are recorded at cost, less accumulated depreciation. Depreciation is calculated on a straight-line basis. Based on the useful lives of fixed assets, the following rates are applied:

Intangible assets	20%
Furniture and equipment	20%
Computers	25%
Other	20%

Gains and losses on disposals of fixed assets are recognised in the profit and loss statement in the period of disposal.
Useful lives, residual values and depreciation methods are reviewed annually.

(14) Cash and cash equivalents

Cash and cash equivalents are composed of cash and amounts due from the Bank of Latvia and other credit institutions on demand, and deposits in other credit institutions with a maturity less than 3 months less balances due to other credit institutions with a maturity less than 3 months.

(15) Off-balance-sheet items

Off-balance-sheet items include guarantees, letters of credit and unused credit lines provided to customers as well as unused limits of credit cards.

(16) Corporate income tax

Corporate income tax at the rate of 15% is calculated by the Bank in accordance with the Latvian tax regulations.

Deferred tax is recognized using the balance sheet liability method, taking into account temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax calculated is based on the expected manner of realization or settlement of the carrying amount of assets and liabilities, using tax rates applied or substantially applied at the balance sheet date.

The deferred tax asset is acknowledged only in those cases when the expected taxable profit is likely to be reduced through the usage of temporary differences.

A deferred tax asset is recognized only to the extent that it is probable that future taxable profits will be available against which the asset can be utilized. Deferred tax assets are reduced by the amount that is not probable that the related tax benefit will be realized.

(17) Provisions

A provision is recognised in the balance sheet when the Bank has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

(18) Assets under management

Assets managed by the Bank on behalf of customers are not treated as assets of the Bank. The Bank assumes no risk on the assets.

A significant amount of managed assets are involved in repurchase (repo) transactions with other commercial banks. The Bank discloses on the balance sheet amounts due to credit institutions for cash received in repo transactions and the amounts due from the providers of liabilities under management as loans granted.

(19) Repo transactions

Repo transactions are recognized as financing transactions.

When the Bank is the seller of securities, securities are continued to be recognized on the balance sheet. Proceeds from the sale are recognized as a liability to the purchaser of the securities.

When the Bank is the purchaser of securities, the purchased securities are not recognized on the balance sheet. The amount paid for securities is recognized as a loan provided to the seller. The Bank is involved in two types of such transactions – classic repo and buy/sell back transactions.

The result of repo and buy/sellback transactions is recognized in the profit and loss statement as interest income or expense according to the accrual principle.

(20) Net profit from insurance

Net profit from insurance (is included in another operating income) includes earned insurance premiums, changes in life insurance reserves less reinsurer's part in such changes in life insurance reserves, and insurance claims paid less reinsurer's part in such insurance claims paid.

Net earned premiums are obtained from subscribed premiums less amounts transferred to reinsurers and changes in unearned premium reserves. Subscribed premiums under life insurance contracts with regular payments are equal to the total premium for the current insurance year regardless of their payment dates. Subscribed premiums are decreased by the premiums cancelled and terminated over the accounting year. Insurance receivables, which result from the difference between subscribed and received premiums, are included in loans. Subscribed premiums under life insurance contracts with non-regular payments are recognized as of the moment of their receipt and are equal to the received premiums.

Insurance claims paid are calculated as claims paid less gross reinsurer's share.

The concern maintains investment assets on a continuous basis in order to cover its insurance liabilities under insurance contracts. Such investment assets include investment securities at their fair value with revaluation result included in the profit and loss account, and investment properties. Income from such investment assets is disclosed in the relevant items of the consolidated profit and loss account. Insurance sales commissions paid out to sales agents and brokers are included in expenses for the period when the same are incurred. They are included in the fees and commissions expenses. Administrative expenses, including payments to the Financial and Capital Market Commission and the Insured Protection Fund, as well as depreciation are disclosed in the relevant items of the consolidated profit and loss account.

(21) Insurance liabilities

Insurance liabilities that result from life and accident insurance contracts are composed of life insurance reserves, reserves for unearned premiums and unpredictable risks, and reserves for deferred insurance claims.

Life insurance reserves reflect existing liabilities against insurants under life insurance contracts. Life insurance reserves are determined for each life insurance contract according to calculations made by actuaries. Prospective method is applied to contracts with regular payment schedule (the reserve equals the difference between the present value of the insurer's liabilities and the present value of future premium income). Retrospective method is applied to contracts with non-regular payment schedule (reserves equal the amount of paid-in accrued premiums less deductions set out in contracts and plus accrued guaranteed interest pursuant to the contract). Life insurance reserves also include reserves for deferred life insurance claims.

Reserves for unearned premiums and unpredictable risks reflect deferred income from non-life insurance contracts according to the share of gross subscribed premiums that refers to the period from the balance sheet date to the end date of insurance contracts, in order to cover all claims and expenses related to existing insurance contracts.

Reserves for deferred claims reflect the amount of claims that have been filled but have not been paid out, as well as the amount of claims that have been assessed and have occurred but have not been filled. Claims reserves are also formed for direct expenses for claims settlement that will be required for settlement of insurance events that have occurred over the accounting and earlier years.

(22*)* Basis for comparison

When necessary the previous financial year's indicators have been reclassified to be comparable with those for the reporting year.

3. RISK MANAGEMENT

The Bank pays significant attention to risk identification and management. The most significant risks to which the Bank is exposed to are credit risk, interest rate risk, liquidity risk, foreign exchange risk, operational and reputational risk.
Risk management principles are set forth in the Bank's risk management policies, which are approved by the Council. Financial Analysis and Risk Management Department, the Asset and Liability committee, Credit committee and Anti Money Laundering committee are responsible for ensuring the implementation of the risk management policies.

(1) Credit risk

Credit risk is the risk of potential losses resulting from non-fulfilment of contractual obligations by the Bank's debtor or counterparty.
Credit risk is managed in accordance with the Credit risk management policy approved by the Council. This policy details the basic principles of credit risk management, identification, assessment, restriction and control.

The management of risks related to ordinary loans involves assessment of the potential borrower's credit standing that is performed by the Financial Analysis and Risk Management Department. Decisions on granting loans are made by the Credit Committee based on the above analysis and evaluation of collateral. Subsequent to loan granting, the Financial Analysis and Risk Management Department performs a regular analysis of the borrower's financial position, which enables the Bank to take prompt action in the case of deterioration of the borrower's financial position.

Credit risk that is related to inter-bank operations (or operations with financial institutions), including the credit risk related to inter-bank settlements, is controlled by the Asset and Liability Committee that sets limits for transactions with each counter party.

The Bank monitors the concentration of significant balance sheet and off balance items' credit risk by geographical regions (i.e., countries, groups of countries, specific regions within the countries etc), client groups (i.e., central governments, local authorities, state enterprises, private enterprises, private individuals, etc) and industries.

(2) Foreign exchange risk

Foreign exchange risk is the risk of potential losses as a result of the revaluation of balance sheet and off-balance sheet items denominated in foreign currencies.
The Bank continuously monitors the open positions of foreign currencies and regularly assesses the structure of assets and liabilities by currency. In order to improve the currency structure of its balance sheet, the Bank issued bonds in EUR currency, taking into account the increasing share of EUR denominated assets.
The Asset and Liability Committee sets limits for the open position in each currency providing an acceptable overall level of foreign currency risk.

(3) Interest rate risk

Interest rate risk is the risk of potential losses the Bank may incur as a result of interest rate fluctuations.
For the purpose of controlling the interest rate risk, the Asset and Liability Committee performs regular analysis of assets and liabilities by maturity and type of interest.

(4) Liquidity risk

Liquidity risk is the risk of potential losses as a result of sales of assets or acquisition of resources at unfavourable prices in order for the Bank to fulfil its liabilities to creditors.
Liquidity risk management is based on the analysis of the structure of assets and liabilities performed by the Bank's Financial Analysis and Risk Management Department. That includes the analysis of dynamics in customer funds by customer group and assessment of the possibilities of external borrowing. Based on this information, the Asset and Liability Committee monitors the Bank's ability to fulfil all its commitments. Operating short-term liquidity management, i.e. attraction and placement of resources, in the Bank is performed by the Resources Department of the Bank based on the short-term liquidity forecast.

(5) Country risk

Country risk is the risk of potential losses arising from transactions with residents of foreign countries (or their securities) due to changes in the economic, political, and legal environment of the respective countries.
Before entering into transactions with residents of foreign countries, the Bank performs an assessment of the influence of economic, social, political and legal circumstances on the residents' ability to fulfil their obligations.

(6) Operational risks

The Bank's organizational structure, precise job specifications, clear division of responsibilities as well as control procedures allow the Bank to monitor operational risks. The Bank has also developed an action plan for various crisis situations.
The Bank has set up an independent "Internal audit service" (IAS) with its main functions to ensure that the Bank's activities comply with existing legislation, approved plans, policies and other internal Bank documents and to monitor the compliance of the Bank's department activities with internal control procedures.

(7) Reputational risk

The Bank recognizes the importance of preventing of money laundering and preventing of terrorism financing. Reputation risk management department was set up in the Bank to implement an internal control system, which monitors the timely control of clients and their business partners. IAS regularly monitors execution of money laundering and terrorism financing prevention policy and procedures.

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