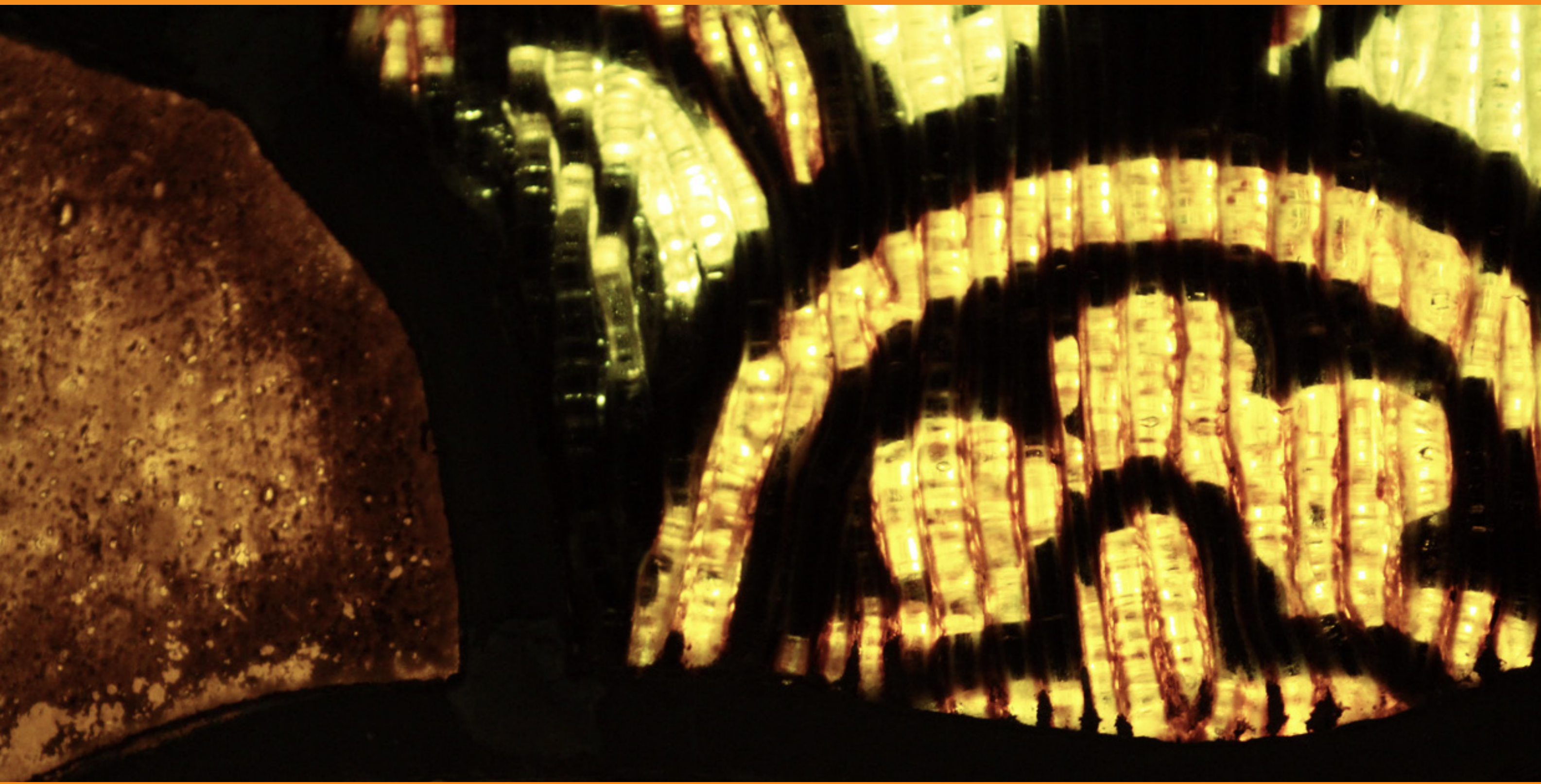
Baltikums Bank



BALTIKUMS BANK AS

II Quarter
2013 Interim Report

(translated from Latvian)

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Background

Baltikums Bank AS (hereinafter referred to as Baltikums Bank or Bank) is a credit institution regulated by the Finance and Capital Markets Commission (Kungu iela 1, Riga, LV-1050, Latvia) and registered with the Register of Enterprises of the Republic of Latvia on 22 June 2001, registration No. 40003510 60. The registered office of the Bank is at Smilsu iela 6, Riga, LV 1050, Latvia.

Baltikums Bank operates in accordance with the applicable legislation of the Republic of Latvia and a license issued by the Bank of Latvia. Its shareholders (beneficial owners) are natural persons resident within the Republic of Latvia.The Bank was founded in Latvia but is also a European and international financial institution. The Bank's primary lines of business are managing the capital of high net worth individuals, banking, investment and advisory service for large and medium-sized businesses and financial institutions.

Baltikums Bank has its head office in Riga (Latvia), with representative offices in Almaty (Kazakhstan), Limassol (Cyprus) and Kiev (Ukraine). The shareholder of Baltikums Bank also holds related companies in Moscow, St. Petersburg (Russia), Bishkek (Azerbaijan), Baku (Azerbaijan) and Luxemburg.

The Group's consolidated and the Bank's separate financial statements for the 12 months of the year 2012 have been prepared in accordance with International Financial Reporting Standards adopted by the European Union, on a going concern basis. Audit was conducted by KPMG Baltics SIA, reg. No. 40003235171. Registered office: 7 Vesetas iela, Riga, LV-1013, Latvia.

This interim report has been prepared in accordance with Financial and Capital Market Commission (FCMC) regulation No. 145, "Regulations on Preparation of Public Quarterly Reports of Credit Institutions", and is aimed at providing information on the Bank's financial standing and the results of its operations.

Amounts in financial statements are indicated in thousands of lats (LVL '000), unless specified otherwise.

Share Capital of the Bank

The sole shareholder of Baltikums Bank is AS „BBG", holding 100% of the Bank's voting shares.

The Bank's share capital is LVL 27,756,200.

The share capital of Baltikums Bank consists of 27,756,200 shares.

The nominal value per share is LVL 1.

Council and Board

Council

Aleksandrs Peškovs (Chairman of the Council)

Sergejs Peškovs (Deputy Chairman of the Council)

Andrejs Kočetkovs (Member of the Council)

Board

Dmitrijs Latiševs – Chairman of the Board, CEO

Tatjana Drobina (until 18.06.2013) – member of the Board, CFO

Inga Mukāne – member of the Board, AMLCO

Leonarda Višņevska – member of the Board, CA

Aleksandrs Halturins, member of the Board, CCSO, CRO

Strategy and Mission

Baltikums Bank AS is a leading European private bank and banking group with a business model that is built around Client Relationship Directors (CRDs). CRDs and their teams are supported by a well-developed operations infrastructure, a broad spectrum of wealth management services, an international network of partners and representation at major business and finance centres across Europe and worldwide. The Bank operates with maximum efficiency, generating considerable operational income while maintaining its costs at the lowest level on the Latvian market. The Bank offers banking, investment and advisory services of a high level of quality and consumer value to private customers who want to delegate financial decisions to us and develop sustainable business relations.

The Bank provides an entire range of high-quality banking products and services to its target customers. As a priority, the Bank develops lines of business that correspond to its business model and core competencies, which allow it to leverage its strengths on highly competitive markets and are consistent with the acceptable level of risk.

The Bank's long-term business priorities are advisory, banking and investment service.

The target customer base of the Bank is consistent with its key development goals:

- high net worth individuals, medium-sized and large companies that require a wide range of services for capital and asset management;
- corporate entities and merchants engaged in international trade and services;
- financial organisations and international investors that require highly professional service for settlement and financial market operations.

The Bank does not plan on providing retail banking services.

Bank Structure

Consolidated Group

No.	Company name and registration No.	Registration country code, registered office	Type of business*	Equity/share of voting rights in company (%)	Reason for inclusion
1.	"BBG" AS 40003234829	LV Mazā Pils iela 13, Riga, LV-1050, Latvia	FMC	100%	Parent company
2.	Baltikums Bank AS 40003551060	LV Smilšu iela 6, Riga, LV-1050, Latvia	BNK	100%	Subsidiary
3.	AS IMC "Baltikums Asset Management" 50003840061	LV Mazā Pils iela 13, Riga, LV-1050, Latvia	IMC	100%	Subsidiary
4.	SIA " Baltikums International" 40003444941	LV Mazā Pils iela 13, Riga, LV-1050, Latvia	OFI	100%	Subsidiary
5.	SIA „CityCap Service" 40003816087	LV Kr.Valdemāra iela 149, Riga, LV-1013, Latvia	OCC	100%	Subsidiary
6.	SIA „ZapDvina Development" 40003716809	LV Kr.Valdemāra iela149, Riga, LV-1013, Latvia	OCC	100%	Subsidiary
7.	Kamaly Development EOOD 147093418	BG Etiera k-s 1/2B - 18, Sveti Vlas, Burgas obl., Nesebier 8256, Bulgaria	OCC	100%	Subsidiary
8.	Rostman Ltd. 56,479	BZ 35 New Road, Belize City, Belize	OCC	100%	Subsidiary
9.	Mateli Estate SIA 50103482941	LV Kr. Valdemāra iela 149-405, Riga, LV-1013, Latvia	OCC	100%	Subsidiary
10.	Darzciems Estate SIA 40103492740	LV Kr. Valdemāra iela 149-405, Riga, LV-1013, Latvia	OCC	100%	Subsidiary
11.	Mazirbe Estate SIA 40103492721	LV Kr. Valdemāra iela 149-405, Riga, LV-1013, Latvia	OCC	100%	Subsidiary
12.	Lielie Zaķi SIA 40103493765	LV Kr. Valdemāra iela 149-405, Riga, LV-1013, Latvia	OCC	100%	Subsidiary
13.	Pulkarne Entity SIA 40103481018	LV Kr. Valdemāra iela 149-405, Riga, LV-1013, Latvia	OCC	100%	Subsidiary
14.	Pils Pakalpojumi SIA 40103170308	LV Kr. Valdemāra iela 149, Riga, LV-1013, Latvia	OCC	100%	Subsidiary
15.	Baltikums Luxembourg S.A. № B 171575, Luxembourg	LU 42, rue de la Vallee, L-2661, Luxembourg	OCC	100%	Subsidiary
16.	Foxtran Management Ltd. № 113,276	BZ Suite 102, Ground Floor, Blake Building, Corner Eyre & Huston Streets, Belize City, Belize	OCC	100%	Subsidiary

Consolidated Group

No.	Company name and registration No.	Registration country code, registered office	Type of business*	Equity/share of voting rights in company (%)	Reason for inclusion
17.	Enarlia International Inc. № 113,273	BZ Suite 102, Ground Floor, Blake Building, Corner Eyre & Huston Streets, Belize	OCC	100%	Subsidiary
18.	Kamaly Development UAB №300558022	LT Klaipedos m. sav. Klaipedos m., Karklu g. 12, Lithuania	OCC	100%	Subsidiary
19.	Baltikums AAS 0003387032	LV Ūdens iela 12 -115, Riga, LV-1007 Latvija	IC	99,72%	Subsidiary
20.	BB Broker Systems SIA 40103670482	LV Aleksandra Čaka iela 92 -2B, Riga, LV-1011, Latvija	OCC	100%	Subsidiary
21.	Jēkaba 2 SIA 40103293621	LV Jēkaba iela 2, Riga, LV-1050, Latvija	OCC	100%	Subsidiary

*BNK – bank, IC – insurance company,
IMC – investment management company, OFI – other financial institution,
FMC – financial management company, OCC – other capital company.

Analysis of Risks

In its activities, Baltikums Bank pays great attention to risk identification and management. The Bank considers the following risks to be substantial for its operations:

- credit risk;
- market risks (securities price risk, interest rate risk in the non-trading portfolio, currency risk);
- liquidity risk;
- operational risks;
- AML (money laundering) risk;
- strategy and business risk.

The Bank's risk management principles are laid out in risk management policies, which have been approved and supervised by its Council. Enforcement of the policies is supervised by the Bank's internal control units:

- Financial Analysis and Financial Risk Management Department;
- Internal Audit Department;
- Customer Activity Compliance Department.

General risk management is ensured by the following committees:

- Credit Committee;
- Assets and Liabilities Committee;
- Money Laundering Prevention Committee.

Credit Risk

Credit risk is the risk of potential loss (or reduced profit) resulting from non-fulfilment of contractual obligations by a customer or counterparty of the Bank, an issuer of securities held by the Bank. It also refers to potential loss (or reduced profit) due to falling prices of securities held by the Bank, or due to impaired credit capacity of the issuer of such securities. For the Bank, credit risk is inherent in issued loans, claims on counterparties, investment in securities and other financial instruments whose price or value depends on a specific legal entity's credit capacity, and in any other claims.

Credit risk is managed in accordance with the Credit Risk Management Policy approved by the Council.

Decisions on granting loans, credit lines, overdrafts and guarantees to customers representing a credit risk for the Bank are made by its Credit Committee The Bank's goals concerning target markets and credit products, crediting provisions, trade financing provisions, credit documentation, and the process of considering and providing loans are specified in the Bank's Credit Policy. Management of credit risk related to loans includes evaluation of the credit capacity of potential borrowers. This is conducted by the Financial Analysis and Financial Risk Management Department, which regularly analyses the financial standing of borrowers following issuance of loans, enabling the Bank and the Group to react to a deterioration of the financial standing of its borrowers in due time. In order to mitigate the extent of credit risk it accepts, the Bank requires borrowers to provide collateral. Collateral is evaluated conservatively; options for selling collateral and controlling it (i.e. securing ownership or management of the collateral) are considered. The credit capacity of insurance companies that insure the subject of collateral is evaluated by the Financial Analysis and Financial Risk Management Department according to the Methodology for Evaluating the Credit Capacity of Insurance Companies.

The credit risk due to transactions of the Bank's Financial Markets Department (interbank loans, Forex transaction claims, loans against securities, purchase of various issuers' bonds, other transactions and storage of funds on correspondent accounts with other banks) is mitigated and controlled at the Bank using limits set by the Assets and Liabilities Committee.

Limits are set on the maximum extent of the Bank's claims on each counterparty (issuer of bonds) with which (whose bonds) transactions take place. The limit system is structured according to the description of the Bank's Limit System, approved by the Assets and Liabilities Committee.

When setting limits, the Assets and Liabilities Committee ensures that sufficient information on the credit capacity of the Bank's counterparty or an issuer of bonds is available for making a decision. The credit capacity of potential institutional counterparties (i.e. banks) is evaluated in accordance with the Methodology for Evaluating the Credit Capacity of Banks. The credit capacity of corporate bond issuers is evaluated according to the Methodology for Evaluating Credit Risk.

Risk Management

Once limits are set for counterparties and issuers of bonds, the Financial Analysis and Financial Risk Management Department regularly monitors their credit capacity according to approved methodologies.

Limits intended for controlling credit risk are supervised according to the Procedure for Controlling Observance of Counterparty Limits, which, among other things, defines the actions of Bank employees when exceedance of limits is identified or when a counterparty fails to fulfil its obligations to the Bank. Evaluation of credit risk takes place by calculating discounted cash flows, modelling various scenarios of potential changes in the value of collateral and possible insolvency cases, which includes stress scenarios.

As of 30.06.2013, the amount of provisions for depreciation of asset value was LVL 1.5 mio.

Currency Risk

Currency risk is the risk of potential losses (or reduced profit) for the Bank due to exchange rate fluctuations. The Bank faces currency risk from having claims and obligations structured in a way that is not balanced across currencies. In line with its Currency Risk Management Policy, the Bank aims for the lowest currency risk possible. The Bank has set limits on open positions in specific currencies as well as the overall open position in foreign currencies in order to manage its currency risk.

To mitigate currency risk, the Bank relies on derivative financial instruments, i.e. currency swap and forward transactions. Based on conservative limits on open currency positions and frequent changes in the structure of open currency positions, the Bank relies on stress-testing methods to evaluate currency risk.

Interest rate Risk

Interest rate risk is the risk of potential losses (or reduced profit) for the Bank due to changes in interest rates at which the Bank borrows or places its resources. Interest rate risk arises due to different dates and currencies being set for "revising" interest rates on the Bank's assets and liabilities. The Bank applies the Monte Carlo simulation method to model potential interest rate changes and evaluate the respective potential for changes in pure interest income.

Securities Price Risk

Securities price risk stems from the Bank's trading portfolio, which consists of debt securities and equity. The Bank applies both the value-at-risk method and stress-testing to evaluate risks. It resorts to various limits to mitigate risks – on the volume of portfolios, on specific issuers, on the duration of the securities portfolio.

Liquidity Risk

Liquidity risk is the risk of potential losses (or reduced profit) for the Bank as a result of sale of assets or acquisition of resources at unfavourable prices in order for the Bank and the Group to fulfil their liabilities to creditors and depositors. Liquidity risk is caused by temporally unbalanced structuring of the Bank's claims and obligations.

Liquidity risk management is regulated by the Bank's Liquidity Risk Management Policy and consists of several elements:

- a system of liquidity risk indicators;
- cash flow planning;
- evaluation and planning of stable resources;
- stress-testing.

In order to calculate potential losses due to liquidity risk, the Bank regularly conducts stress-testing using both historic and hypothetical scenarios. The main scenario is a combined scenario consisting of a crisis for the Bank and for the market in general, which factors in considerable withdrawal of deposits and considerably reduced liquidity on the securities market. Stress-testing forecasts the potential liquidity situation, and the Bank's asset structure is shaped so as to allow the Bank to fulfil its obligations to creditors even in a crisis situation.

Operational Risk

Operational risk denotes the possibility of direct or indirect losses caused by uncontrollable events which occur due to flaws in the organisation of

Risk Management

business, inadequate control, incorrect decision-making, system errors related to human factors, technology, property, internal systems, the impact of internal and external factors, legal regulation, and certain projects. The Bank regularly evaluates the probability of occurrence of operational risk identified for all crucial products, lines of business, processes and systems, as well as the impact of this risk of the Bank's operations under internal regulations developed by the Operational Risk Management Department and approved by the Board. Operational risk self-assessment methodology is used to evaluate the risk.

In order to ensure the Bank's ability to maintain operations and reduce losses in emergency situations, the Bank develops an operational continuity plan, identifying the processes and resources essential for its activity (which must therefore be restored immediately in case of faults and operational interruptions) and defines technical measures and activities as part of labour organisation and ways of restoring essential processes and resources.

Money Laundering Risk

Money laundering risk is the risk of lacking compliance of the Bank's activity to money laundering prevention regulations, or the Bank's involvement in money laundering and/or terrorist financing through its customers or counterparties. In order to manage this risk, the Bank identifies business processes subject to this risk, ensures supervision of such processes, applies acknowledged international standards and provides the necessary information technology and training of employees. The Bank's money laundering risk is managed by the Customer Activity Compliance Department and by certain committees.

Strategy and Business Risk

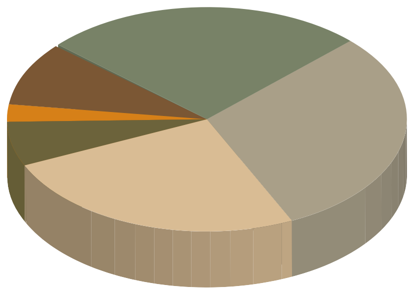
Strategy and business risk denotes the Bank's potential losses due to operation according to the strategy it has selected, which may prove erroneous or inadequate considering internal resources or external conditions.

In order to manage strategy risk, the Bank has defined a strategy, formulated its mission, primary lines of business and products, target market and customer base, as well as developed a planning system to analyse various scenarios of development conditional on the development of external trends, and an external system for controlling fulfilment of plans.

The Bank identifies risks attributable to the selected strategy and develops the relevant methods for managing them (mostly on the basis of scenario analysis), or else considers them as part of managing other substantial risks. The Bank's management is in charge of managing the strategy and business risk.

Exposure to risks

At the end of the reporting period, the Bank's equity was sufficient to cover the potential risk of loss (which is assessed using an internal methodology). The Bank's risk coverage capital is structured as shown below:



- 26.4% credit risk related to interbank claims (excluding bonds)
- 30.2% credit risk related to loans extended to customers
- 25.2% credit risk related to investment in bonds and to loans secured by bonds
- 6.4% credit risk related to other assets
- 2.7% market risks
- 9.2% operational risk

Profit and Loss Account

30 June 2013

Item	30.06.2013 LVL'000	30.06.2012 LVL'000
Interest income	2 439	2 634
Interest expenses	(521)	(475)
Dividend income	43	98
Fee and commission income	6 548	5 172
Fee and commission expenses	(544)	(500)
Net realised gain/loss from financial assets and financial liabilities carried at amortised cost	0	0
Net gain/loss from available-for-sale financial assets and financial liabilities	0	0
Net gain/loss from held-for-trading financial assets and financial liabilities	(141)	552
Net realised gain/loss from financial assets and financial liabilities carried at fair value through profit or loss	0	0
Changes in fair value in risk mitigation accounts	0	0
Gain/loss from trading and revaluating foreign currencies	1 988	1 646
Gain/loss from ceasing recognition of property, equipment and appliances, investments in property and intangible assets	0	0
Other income	85	40
Other expenses	(173)	(213)
Administrative expenses	(4 486)	(3 475)
Depreciation	(107)	(109)
Net result of creating reserves	(339)	(1 248)
Recovery of written-off assets	0	1
Profit before corporate income tax	**4 792**	**4 123**
Corporate income tax	(779)	(595)
Profit for reporting period	**4 013**	**3 528**

Balance Overview

30 June 2013

Item	30.06.2013 LVL'000	31.12.2012 LVL'000
Cash and on-demand claims on central banks	65 515	34 690
On-demand claims on credit institutions	142 879	133 397
Financial assets held for sale	23 111	10 299
Financial assets classified as carried at fair value through profit or loss	0	0
Financial assets available for sale	63	63
Loans and claims, including interbank loans	127 563	91 578
Investments held to maturity	25 377	37 988
Changes in fair value of risk-hedged portfolio	0	0
Accrued income and expenses for subsequent periods	136	67
Fixed assets	234	237
Investment properties	3 420	3 423
Intangible assets	383	184
Investment in the stock capital of related and associated companies	7 926	7 191
Tax assets	0	0
Other assets	9 345	6 046
Total assets	**405 952**	**325 163**
Due to central banks	0	0
Due on-demand to credit institutions	2 402	2 211
Financial liabilities held for trading	84	79
Financial liabilities classified as carried at fair value through profit or loss	0	0
Financial liabilities carried at amortized purchase cost	370 174	292 306
Financial liabilities due to transfer of financial assets	0	0
Liabilities due to changes in the fair value of interest-hedged portfolio	0	0
Accrued expenses and income for subsequent periods	273	304
Reserves	281	216
Tax liabilities	238	523
Other liabilities	140	259
Total liabilities	**373 592**	**295 898**
Capital and reserves	**32 360**	**29 265**
Total capital, reserves and liabilities	**405 952**	**325 163**
Off-balance items		
Potential liabilities	268	542
Off-balance liabilities to customers	10 986	6 829

Equity and Capital Requirement Overview

30 June 2013

No.	Item	For reporting period
1	Stock capital (1.1+1.2+1.3+1.6) or (1.4+1.5+1.6)	29 960
1.1	Tier I capital	27 920
1.2	Tier II capital	3 115
1.3	Reduction in tier I and tier II capital (-)	(1 075)
1.4	Total tier I capital with reduction	27 383
1.5	Total tier II capital with reduction	2 577
1.6	Used tier III capital	0
2	Total capital requirement (2.1+2.2+2.3+2.4+2.5)	14 976
2.1	Total of capital requirements for credit risk, counterparty credit risk, recovered value reduction risk and unpaid delivery risk	12 289
2.2	Capital requirement for settlement/delivery risk	0
2.3	Total of capital requirements for exposure, foreign exchange and commodity risk	719
2.4	Capital requirement for operational risk	1 968
2.5	Total of other and transitional period capital requirements	0
	Additional data	
3.1	Coverage of capital requirements with equity (surplus (+) or deficit (–)) without the total of other and transitional period capital requirements = 1–(2–2.5)	14 984
3.1.a	Capital adequacy ratio (%),without the total of other and transitional period capital requirements = 1/(2–2.5)*8%	16.00
3.2	Coverage of capital requirements with equity (surplus (+) or deficit (–)) = 1–2	14 984
3.2.a	Capital adequacy ratio =1/2*8%	16.00

Operational Performance

30 June 2013

Item	30.06. 2013	30.06. 2012
Return on equity (ROE) (%)	25.44	28.79
Return on assets (ROA) (%)	1.97	2.67

Securities Investments

Investments in securities by country (exceeding 10% of equity)

Issuer's country	Value (LVL)	Coupon (LVL)	Accruals (LVL)	Subtotal (LVL)
Kazakhstan	5 718	181	0	5 899
Russia	20 722	448	0	21 170
U.S. central government	8 085	0		8 085
International development banks	5 366	49	0	5 415
Other countries	6 914	194	(5)	7 103
Including central governments	*3 596*	*128*	*0*	*3 724*
TOTAL	**46 805**	**872**	**(5)**	**47 672**

Dmitrijs Latiševs
Chairman of the Board
CEO

Contact details

Address: Smilšu iela 6, Riga, LV-1050, Latvia
Phone: +371 67 031 311
Fax: +371 67 031 300
E-mail: info@baltikums.eu
Internet: www.baltikums.eu
SWIFT code: CBBRLV22