Information disclosed in the report is prepared in accordance with the Financial and Capital Market Commission's regulations No. 145 "Regulations on Preparation of Public Quarterly Reports of Credit Institutions".

Unaudited financial and operating results in the 1st quarter of 2010

During the 1st quarter of 2010, the main focus of *Parex banka's* management was on the restructuring of the Bank. On 25 January, the state joint stock company (JSC) *Privatizācijas aģentūra*, or Latvian Privatization Agency (LPA) and *Parex banka* signed a service agreement with the international consulting firm *Nomura International plc*, under which a restructuring plan was drawn up for *Parex banka*. On 23 March, the Latvian Cabinet of Ministers (Government) approved this restructuring plan, according to which part of *Parex banka's* assets will be used for the creation of a new bank. The main beneficiaries will be the depositors in the current *Parex banka*, as their deposits will be automatically transferred to the new bank. The soon-to-be-created bank will have a stable financial base, which will make it easier to attract investors and repay the resources invested into the Bank by Latvian state institutions at the earliest possible convenience. The principal restructuring goals of the Bank are to stabilize the enterprise's operational activities, create a stable bank with long-term potential, and increase the interest of private investors in the bank. The Resolution bank, for its part, will be able to sell its assets in the market over the long term, with the goal of ensuring a maximum return on the investment made by Latvian state structures. By supporting the main operations of *Parex group*, a further impetus will also be given to the recovery of the Latvian economy.

Furthermore, during the 1st quarter of 2010, *Parex banka* received the authorization of the International Monetary Fund and the Latvian Financial and Capital Market Commission (FCMC) to increase the credit limits of the Bank's largest, loyal corporate clients. The Bank also signed an agreement with the European Investment Bank on the granting of EUR 100 million in credit resources for loans to small and medium enterprises, and signed a trade finance agreement with the European Bank for Reconstruction and Development (EBRD).

Parex banka's liquidity is improving and currently its liquidity ratio already exceeds 60%. During the first three months of this year, the volume of deposits in the Bank continued to increase and compiled data indicate that the total volume of deposits at the end of March exceeded EUR 1.4 billion, not including the deposits placed into the Bank by the State Treasury. Since the beginning of this year, the total volume of client deposits in the Bank and in the Group has grown by EUR 186.7 million and EUR 213.1 million, respectively. Although an increase in deposits can be observed in all of the Bank's business segments, the largest increase of EUR 84.7 million has been in the corporate client segment. In accordance with the terms of its agreements, *Parex banka* has paid out more than EUR 72.6 million in interest payments to the State Treasury since December of 2008 for term deposits placed by the State Treasury into the Bank.

On 12 February 2010, the Bank repaid a scheduled, syndicated loan tranche of EUR 310 million. Thanks to the Bank's improved liquidity indicators, the Bank was able to provide the majority of this sum, or EUR 165 million, on its own. The remaining EUR 145 million were covered by the State Treasury in the form of a term deposit in the Bank. On 15 February 2010, the *Parex banka* concluded its first issue of debt securities amounting to EUR 17.7 million, and signed two-year deposit agreements to the tune of EUR 130 million. These measures were undertaken in the process of restructuring Bank's deposits that are subject to restrictions, thus further reducing the balance figures of such deposits and improving the Bank's liquidity indicators.

On 31 March 2010, the *Parex banka's* loan portfolio was EUR 2.02 billion, while that of the Group was EUR 2.31 billion. Total assets amounted to EUR 3.48 billion for the Bank and EUR 3.68 billion for the Group. The volume of capital and reserves was EUR 228.1 million for the Bank and EUR 202.4 million for the Group at the end of the 1st quarter of 2010. During the first three months of 2010, the Bank continued to comply with the Latvian regulations governing capital requirements. The Latvian state, as the Bank's largest shareholder, continued to support the Bank by providing it with an additional, required volume of capital. On 23 February 2010, the Latvian Cabinet of Ministers approved an increase of EUR 44.8 million in the *Parex banka's* equity capital. On 26 February 2010, the capital increase was carried out by capitalizing the respective amount of from the existing State Treasury deposits with the Bank.

The Bank and the Group ended the 1st quarter of this year with total, net losses of EUR 38.0 million and EUR 43.8 million, respectively. However, loss before provisions, depreciation and tax was EUR 14.0 million for the Bank and EUR 15.0 million for the Group. The financial results continued to be largely affected by provisions to cover a loss in asset value – EUR 27.0 million for the Bank and EUR 29.7 million for the Group.

The most recent compiled data indicate that during the 1st quarter of this year, in comparison with the 4th quarter of 2009, *Parex banka* reduced its operational expenses by 13% or EUR 2.4 million. Property management and utility expenses decreased by EUR 0.7 million, communication and IT expenses fell by EUR 0.4 million, personnel costs by EUR 0.4 million, etc. Part of these expenses were reduced by contracting out a number of services to third-party providers. For example, the property management costs of a number of Bank branches will thus be reduced by 80%, while those of office and general supplies will decrease by 22%. A number of other projects have been initiated to provide further cost savings over the long term. For example, new data transmission lines are being installed to connect the Bank’s various branches and its automated teller machines. These lines are not only faster and more secure, but will also provide the Bank with the opportunity to save EUR 0.7 million over a three-year period.

Significant events after the end of the reporting period

Shortly after the end of the reporting period, in April of this year, *Parex banka* received an award as one of the highest customer-rated enterprises in the finance sector, drawing 23 917 client compliments during the *Give praise to good service!* (*Uzslavē labu servisu!*) campaign. In Riga the *Laimdota* and *Citadele* bank branches received the most praise from their clients, while outside of Riga the most popular client centres were in Daugavpils, Gulbene, Rēzekne, Saldus and Jēkabpils. Clients were particularly pleased with the individual approach and friendly service provided by the Bank’s client service specialists.

New Council of *Parex banka* was elected during extraordinary meeting of shareholders on 6 April 2010. Following Council members were elected – Juris Jākobsons, Michael J. Bourke, Laurence Phillips Adams, Juris Vaskāns and Klāvs Vasks. Two new representatives were elected to the Council – Juris Jākobsons, Project Manager of *Parex banka* restructuring issues at *Latvian Privatisation Agency*, and Klāvs Vasks, Member of the Board at *Latvian Guarantee Agency*. Both appointed Council Members have more than 15 years of extensive experience in banking sector. Representatives of Ministry of Finance Andžs Ūbelis and Kaspars Āboliņš have resigned from *Parex banka’s* Council effective 31 March 2010. Both former Members of *Parex banka’s* Council did not receive any financial awards for efforts in the Bank’s Council and will not receive any compensations for the resignation.

On 29 March 2010 *Parex banka* concluded an agreement on sale of Bank’s subsidiary company *Parex Leasing* in Belarus. The deal was closed on 5 May 2010. As a result of this deal *Parex banka* has disposed of a part of assets, which are not in line with its business targets. According to Bank’s strategy, its basic activities are focused on the Baltic market.

In May, *Parex banka’s* daughter company *Parex līzings un faktorings* resumed leasing services to clients. Financing is now available to both private individuals and legal entities. Clients have the opportunity to obtain motor vehicles through either financial or operative leasing.

On 5 May 2010, *Parex banka* concluded an agreement with the *Bank of Latvia* on repayment of loans amounting to EUR 167.3 million prior to final maturity. This decision was made taking into account the constantly growing deposit base of *Parex banka*, the stability in the LVL money market, as well as the fact that the Bank’s liquidity indicators significantly exceed the minimum requirements.

During the forthcoming months, *Parex banka's* main priority will be to bring its restructuring process to a successful conclusion. Once *Parex banka's* restructuring process has been completed, the New Bank will be able to fully devote its efforts to expanding its client base and increasing its earnings.

Information disclosed in the report is prepared in accordance with the Financial and Capital Market Commission's regulations No. 145 "Regulations on Preparation of Public Quarterly Reports of Credit Institutions".

BALANCE SHEETS AS AT 31 MARCH 2010 AND 31 DECEMBER 2009

EUR 000's

	Reporting period *Unaudited*	**Preceding reporting year** *Audited**	**Reporting period** *Unaudited*	**Preceding reporting year** *Audited**
	Group	**Group**	**Bank**	**Bank**
Cash and demand deposits with central banks	342 608	224 105	320 355	202 416
Demand deposits with credit institutions	199 726	296 662	191 618	261 568
Financial assets held for trading	4 223	6 780	4 199	6 793
Financial assets designated at fair value through profit and loss	3 476	3 941	-	-
Available-for-sale financial assets	148 606	162 704	116 512	135 456
Loans and receivables to customers:				
Loans to credit institutions	71 339	17 560	204 714	202 102
Loans to companies and private individuals	2 306 911	2 362 491	2 017 793	2 056 627
Held-to-maturity investments	408 373	425 966	422 454	453 397
Prepayments and accrued income	6 152	6 574	4 550	5 021
Fixed assets	71 693	74 694	16 449	17 850
Intangible assets	4 425	4 687	703	832
Investments in subsidiaries	-	-	103 145	103 479
Investment property	2 279	1 249	-	-
Income tax assets	50 412	56 159	45 963	51 211
Other assets	60 116	51 480	28 230	19 378
Total assets	**3 680 339**	**3 695 052**	**3 476 685**	**3 516 130**

Due to central banks	193 377	238 994	193 377	238 994
Demand liabilities to credit institutions	1 000	875	17 473	10 165
Financial liabilities held for trading	1 087	1 333	1 096	1 369
Financial liabilities designated at fair value through profit and loss	1 140	1 009	-	-
Financial liabilities measured at amortised cost:				
Loans from credit institutions	238 869	546 219	246 105	565 836
Deposits from customers	2 714 895	2 401 593	2 479 007	2 192 174
Issued debt securities	149 349	128 842	149 397	129 114
Subordinated liabilities	148 040	147 906	148 048	147 916
Other financial liabilities	7 443	7 726	-	-
Accrued expenses and deferred income	8 752	8 435	7 375	7 150
Income tax liabilities	916	1 824	-	-
Other liabilities	13 085	12 587	6 709	6 183
Total liabilities	**3 477 953**	**3 497 343**	**3 248 587**	**3 298 901**
Shareholders' equity	202 386	197 709	228 098	217 229
Total liabilities and shareholders' equity	**3 680 339**	**3 695 052**	**3 476 685**	**3 516 130**

Memorandum items				
Contingent liabilities	8 765	9 713	15 563	16 312
Financial commitments	147 402	179 407	188 898	236 656

* Auditors: SIA „PricewaterhouseCoopers"

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STATEMENTS OF INCOME
FOR 3 MONTHS PERIOD ENDED 31 MARCH 2010 AND 31 MARCH 2009

EUR 000's

	Reporting period *Unaudited*	Respective period of the preceding reporting year *Unaudited*	Reporting period *Unaudited*	Respective period of the preceding reporting year *Unaudited*
	Group	**Group**	**Bank**	**Bank**
Interest income	37 779	80 862	33 447	71 908
Interest expense	(43 116)	(58 813)	(41 266)	(57 372)
Dividends received	3	26	1 248	26
Commission and fee income	9 139	10 723	6 833	8 347
Commission and fee expense	(2 607)	(3 115)	(2 100)	(2 612)
Net gain/ (loss) on available for sale financial assets and financial liabilities	968	(1 039)	(46)	-
Net gain/ (loss) on financial assets or financial liabilities designated at fair value though profit and loss	(649)	(630)	(660)	(598)
Net gain/ (loss) on held for trading financial assets and financial liabilities	176	3 507	178	3 495
Gain/ (loss) from foreign exchange trading and revaluation of open positions	1 486	95	600	(131)
Net gain/ (loss) on disposal of non-current assets held for sale	(1 086)	-	-	-
Other income	3 836	5 489	2 222	4 180
Other expense	(212)	(337)	(64)	(219)
Administrative expense	(20 683)	(30 750)	(14 446)	(22 598)
Amortisation and depreciation charge	(3 413)	(3 695)	(1 481)	(2 525)
Impairment charge and reversals, net	(29 658)	(17 228)	(27 019)	(11 170)
Corporate income tax	4 230	(647)	4 570	(640)
(Loss)/ profit for the reporting period	**(43 807)**	**(15 552)**	**(37 984)**	**(9 909)**

Statements of Comprehensive Income:

EUR 000's

	01.01.2010.- 31.03.2010.	01.01.2009.- 31.03.2009.	01.01.2010.- 31.03.2010.	01.01.2009.- 31.03.2009.
	Grupa	**Grupa**	**Banka**	**Banka**
Net change in fair value revaluation reserve of securities	3 665	(181)	4 032	(172)
Other comprehensive income / (loss) for the period	**3 665**	**(181)**	**4 032**	**(172)**

Total comprehensive income / (loss) for the period	**(40 142)**	**(15 733)**	**(33 951)**	**(10 081)**

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PERFORMANCE RATIOS OF THE GROUP AND THE BANK

	Reporting period	Respective period of the preceding reporting year	Reporting period	Respective period of the preceding reporting year
	Group	Group	Bank	Bank
Return on equity (ROE) (%)*	(87.59)	(59.45)	(68.24)	(37.67)
Return on assets (ROA) (%)*	(4.75)	(1.35)	(4.35)	(0.89)

* Average value is calculated as the arithmetic mean of the balance sheet assets or residual capital and reserves at the beginning of the reporting period and at the end of the reporting period.

RATINGS ASSIGNED BY RATING AGENCIES

	Long-term raiting	Short-term rating	Financial strength rating	Support rating	Rating’s outlook
Moody's Investors Service	B2	Not Prime	E	-	Developing
Fitch	RD	RD	F	5	*

* Outlook for this rating is not assigned.

Detailed information about ratings can be found on the web sites of the rating agencies: www.moodys.com; www.fitchratings.com

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CONSOLIDATION GROUP

No.	Name of company	Registration number	Registration address	Country of domicile	Company type*	% of total paid-in share capital	% of total voting rights	Basis for inclusion in the group**
1	AS “Parex banka"	LV-40003074590	Latvia, Riga LV-1010, Republikas laukums 2A	LV	BNK	100	100	MAS
2	IPAS "Parex Asset Management"	LV-40003577500	Latvia, Riga LV-1010, Republikas laukums 2A	LV	IPS	100	100	MS
3	Regalite Holdings Limited	CY-HE93438	Cyprus, Nicosia 1075, 58 Arch. Makarios 3 Avenue, Iris Tower, 6th floor, office 602	CY	PLS	100	100	MS
4	AB "Parex bankas"	LT-112021619	Lithuania, Vilnius LT-03107, K. Kalinausko 13	LT	BNK	100	100	MS
5	SIA "Parex Express Kredīts"	LV-40003238125	Latvia, Riga LV-1010, Republikas laukums 2A	LV	CFI	100	100	MS
6	AS "Parex atklātais pensiju fonds"	LV-40003397312	Latvia, Riga LV-1010, Republikas laukums 2A	LV	PFO	100	100	MS
7	AAS "Parex Dzīvība"	LV-40003786859	Latvia, Riga LV-1010, Republikas laukums 2A	LV	APS	100	100	MMS
8	OU "Parex Leasing & Factoring"	EE-10925733	Estonia, Tallinn 10119, Roosikrantsi 2	EE	LIZ	100	100	MS
9	ZAO "Parex Asset Management"	RU-1037706024872	Russia, Moscow 119049, Donskaja 4 - 2	RU	IBS	100	100	MMS
10	OOO “Parex Asset Management Ukraina”	UA-32984601	Ukraine, Kiev 01034, Glibocicka 17	UA	IBS	100	100	MMS
11	SIA "E & P Baltic Properties"	LV-40003754637	Latvia, Riga LV-1010, Republikas laukums 2A	LV	IPS	50	50	MMS
12	UAB "Parex faktoringas ir lizingas"	LT-126233315	Lithuania, Vilnius LT03107, K.Kalinausko 13	LT	LIZ	100	100	MMS
13	UAB "Parex investiciju valdymas"	LT-111829843	Lithuania, Vilnius LT01109, Gyneju 16	LT	IBS	100	100	MMS
14	AP Anlage & Privatbank AG	CH-130.0.007.738-0	Switzerland, Freienbach 8807, Kantonsstrase 1	CH	BNK	100	100	MS
15	OOO "Parex Leasing and Factoring"	AZ-1105-T10-3749	Azerbaijan, Baku AZ1065, Dz.Dzabbarli 44, "Caspian Plaza"	AZ	LIZ	100	100	MS
16	OOO "Ekspress Lizing"	RU-1037867006726	Russia, St. Petersburg 192019, Sedova 11, liter A	RU	LIZ	100	100	MS
17	LLC "Laska Lizing"	UA-33104543	Ukraine, Kiev 03150, Dimitrova 5	UA	LIZ	100	100	MS
18	LLC "Parex Leasing"	RU-1047796715603	Russia, Moscow 111116, Energeticheskaja 3	RU	LIZ	100	100	MS
19	IOOO "Pareks Lizing"	BY-190567618	Belarus, Minsk 220007, Libavoromenskaja 23	BY	LIZ	100	100	MS
20	OOO "Extroleasing"	RU-1027739537220	Russia, Moscow 111116, Energeticheskaja 3	RU	LIZ	100	100	MS
21	Calenia Investments Limited	CY-HE156501	Cyprus, Nicosia 1075, 58 Arch. Makarios 3 Avenue, Iris Tower, 6th floor, office 602	CY	PLS	100	100	MS
22	SIA "Parex Līzings un faktorings"	LV-50003760921	Latvia, Riga LV-1010, Republikas laukums 2A	LV	LIZ	100	100	MS

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No.	Name of company	Registration number	Registration address	Country of domicile	Company type*	% of total paid-in share capital	% of total voting rights	Basis for inclusion in the group**
23	SIA "Rīgas Pirmā Garāža"	LV-40003397543	Latvia, Riga LV-1010, Republikas laukums 2A	LV	PLS	100	100	MS
24	SIA "Parex Private Banking"	LV-40003103438	Latvia, Riga LV-1050, Smilšu 7	LV	PLS	100	100	MS
25	OOO "Extrocredit"	RU-1067746758518	Russia, Moscow 111116, Energeticheskaja 3	RU	CFI	99	99	MMS
26	LLC "Parex Leasing and Factoring"	GE-205224461	Georgia, Tbilisi, Kazbegi avenue 44	GE	LIZ	100	100	MS
27	SIA "RPG interjers"	LV-40103157899	Latvia, Riga LV-1010, Republikas laukums 1	LV	PLS	100	100	MMS
28	SIA "PR Speciālie projekti"	LV-40103195231	Latvia, Riga LV-1010, Republikas laukums 2A	LV	PLS	100	100	MMS
29	OOO "Parex Investments Ukraine"	UA-35726203	Ukraine, Kiev 03150, Gorkovo 172	UA	IBS	100	100	MMS
30	OAO Parex Ukrainian Equity Fund	UA-10681020000023247	Ukraine, Kiev 03150, Gorkovo 172	UA	IBS	100	100	MMS
31	SIA "NIF"	LV-40103250571	Latvia, Riga LV-1010, Republikas laukums 2A	LV	PLS	100	100	MS
32	SIA “NIF Dzīvojamie īpašumi”	LV-40103253915	Latvia, Riga LV-1010, Republikas laukums 2A	LV	PLS	100	100	MMS
33	SIA “NIF Komercīpašumi”	LV-40103254003	Latvia, Riga LV-1010, Republikas laukums 2A	LV	PLS	100	100	MMS
34	SIA “NIF Zemes īpašumi”	LV-40103255348	Latvia, Riga LV-1010, Republikas laukums 2A	LV	PLS	100	100	MMS
35	UAB “Nekilnojamojo turto valdymo fondas”	LT-302462108	Lithuania, Vilnius LT03107, K.Kalinausko 13	LT	PLS	100	100	MMS
36	OÜ “Restruktureeritud Kinnisvarafond”	EE-11788043	Estonia, Tallinn 10119, Roosikrantsi 2	EE	PLS	100	100	MMS

*BNK – bank, IBS – investment brokerage company, IPS – investment management company, PFO – pension fund, CFI – other financial institution, LIZ – leasing company, PLS – company providing various support services, APS – insurance company.
** MS – subsidiary company, MMS – subsidiary of the subsidiary company, KC – joint venture, MAS – parent company.

INFORMATION ABOUT PAREX BANKA’S BRANCHES

As at 31 March 2010 the Bank was operating a total of 23 branches, including 4 foreign branches, 3 small client service centres, 47 mid-size client service centres and 5 representative offices.

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ISSUED SHARE CAPITAL AS AT 31 MARCH 2010

Shareholders	Nominal value (LVL)	Number of shares	Paid-in share capital (EUR)	Voting rights	Paid-in share capital (%)
SJSC "Privatizācijas Aģentūra"	1	200 420 791	285 173 094	144 470 791	76.64%
EBRD	1	51 444 325	73 198 680	51 444 325	19.67%
Other	1	9 662 179	13 748 042	5 468 323	3.69%
Total		**261 527 295**	**372 119 816**	**201 383 439**	**100%**

MANAGEMENT OF THE BANK AS AT 31 MARCH 2010

Council of the Bank

Name	Position
Andžs Ūbelis	Chairman of the Council
Michael Joseph Bourke	Deputy chairman of the Council
Laurence Phillips Adams	Member of the Council
Kaspars Āboliņš	Member of the Council
Juris Vaskāns	Member of the Council

Management of the Bank

Name	Position
Nils Melngailis	President; Chairman of the Management Board, p.p.
Guntis Beļavskis	Member of the Management Board, p.p.
Roberts Stuģis	Member of the Management Board
Vladimirs Ivanovs	Member of the Management Board
Valters Ābele	Member of the Management Board

On 28 January 2010 the previous Supervisory Council of Parex banka was re-elected during an extraordinary meeting of the Bank's Shareholders. The EBRD is represented in Parex banka's Supervisory Council. The following members were re-elected to Parex banka's Council – Andžs Ūbelis, Michael J. Bourke, Laurence Phillips Adams (EBRD nominee), Kaspars Āboliņš and Juris Vaskāns.

INFORMATION ON CERTAIN PARTIES THAT WERE RELATED TO THE BANK AT THE MOMENT IT RECEIVED STATE AID

Pursuant to FCMC regulations On preparation of quarterly public reports of banks (Article 14^1) the following table represents summary of material transactions with certain parties that were related to the Bank at the moment it received the State Aid:

EUR 000's

	1st quarter of 2010			1st quarter of 2009		
	Period-end balance	**Average interest rate ***	**Interest income/ (expense)**	**Period-end balance**	**Average interest rate ***	**Interest income/ (expense)**
Loans issued by the Bank	42 638	2.11%	221	43 494	4.73%	515
Deposits placed with the Bank	39 849	7.90%	(787)	39 850	9.58%	(955)
Subordinated financing provided to the bank	51 233	11.22%	(1 434)	51 229	12.41%	(1 587)

* according to period-end rates

Loan contracts were entered into force in the period from 2002 – 2008 and are maturing in 2018. Loans are USD and EUR denominated.

Deposit contracts were entered into force in 2008 and are maturing in 2011. Deposits are LVL denominated.

Subordinated financing contracts were entered into force in 2008 and have maturities ranging 2015 through 2018. Subordinated financing is LVL and EUR denominated. Prior repayment can be unilaterally requested only upon liquidation of the Bank.

RISK MANAGEMENT

Risk management principles are set out in Group's Risk and Capital Management Policy. The Group adheres to the following key risk management principles:

- The Group aims to ensure an acceptable risk level in all operations. Risks are always assessed in relation to the expected return. Risk exposures that are not acceptable for the Group are avoided, limited or hedged;
- The Group does not assume high or uncontrollable risks irrespective of the return they provide. Risks should be diversified and those risks that are quantifiable should be limited or hedged;
- The Group pursues prudent risk management policy, that is aligned with the Group' business and ensures effective total risk mitigation;
- Risk management is based on awareness of each and every Group's employee about the nature of transactions he/she carries out and related risks;
- Risk limit system and strict controls are essential risk management elements. Control of risk level and compliance with limits is ensured by structured risk limit systems for all material risks;
- The Group aims to ensure low risk exposure, diversified asset portfolio, limited risks in financial markets and low level of operational risk.

Risk management is an essential element of the Group's management process. Risk management within the Group is controlled by independent units - Risk and Compliance Sector.

The Group is exposed to the following main risks: credit risk, market risk, interest rate risk, liquidity risk, currency risk and operational risk. The Group has approved risk management policies for each of these risks, which are briefly summarised below.

Credit risk

Credit risk is the risk that the Group will incur a loss from debtor's non-performance or default. The group is exposed to credit risk in to its lending, investing and trading activities, as well as in respect to the guarantees issued to third parties and other off-balance sheet commitments to third parties.

Credit risk management is based on adequate risk assessment and decision-making. For material risks, risk analysis is conducted by independent units of Risk and Compliance Sector. The analysis of credit risk comprises evaluation of customer's creditworthiness and collateral and its liquidity. The analysis of creditworthiness of a legal entity includes analysis of the industry, the company, and its current and forecasted financial position. The analysis of creditworthiness of an individual includes the analysis of the customer's credit history, income and debt-to-income ratio analysis, as well as the analysis of social and demographic factors. In the event of material risks, lending decision is made by the Credit Committee, and further reviewed by the Bank's Management Board.

After the loan is issued, customer's financial position is monitored on a regular basis in order to timely identify potential credit losses.

To limit its credit risk, the Group has set the following concentration limits: individual counterparty limit, limit for group of mutually related customers, limit for large risk exposures, limit for the Group's related parties, an industry limit, limit by customer type and loan product. As at the date of approval of this report the relevant limits set for the Bank were complied with.

The Group reviews its loan portfolio on a regular basis to assess its quality and concentrations, as well as to evaluate the portfolio trends.

Credit risk identification, monitoring and reporting is the responsibility of Risk and Compliance Sector.

Market risk

Market risk is the risk that the Group will incur a loss as a result of the mark-to-market revaluation of balance sheet and off-balance sheet items caused by changes in market values of financial instruments due to changes in foreign exchange rates, interest rates and other factors.

Position risk of financial instruments is assessed and limits are set by the Financial Market and Counterparty Committee (FMCC). The decisions of FMCC are approved by the Bank's Management Board. Market risk is managed by the Group's business units and subsidiaries which can accept market risk in line with the set limits and investment restrictions of the respective portfolio. Market risk is measured, monitored and risk levels are reported by Risk and Compliance Sector.

To manage market risk, the Group sets individual limits to issuers and financial instruments, as well as products exposed to market risk. To assess position risk the Group also uses scenario analysis.

Interest rate risk

Interest rate risk is related to the negative impact of interest rate changes on the Group's income and economic value.

Interest rate risk management in the Group is carried out in accordance with the Group's Interest rate Risk Management Policy. Interest rate risk is assessed and decisions are made by Assets and Liabilities Management Committee (ALCO). The decisions of ALCO are approved by the Bank's Management Board. ALCO sets the acceptable interest rate risk level and the Group's internal limit system, monitors the compliance with the approved limits and use of the instruments for the management of interest rate risk. Interest rate risk measurement, management and reporting are responsibilities of Treasury Sector. Interest rate risk management in the Group is coordinated by the Risk and Compliance Sector.

The Group manages interest rate risk by using the gap analysis of the risk sensitive assets and liabilities, duration analysis and sensitivity analysis of assets and liabilities as well as stress testing of interest rate risk. Based on the market analysis and the Group's financing structure, ALCO sets customer deposit interest rates. During the period when restrictions are imposed on the Bank's activities, these functions are carried out by the Bank's Management Board.

Liquidity risk

Liquidity risk is the risk that the Group will be unable to meet its legal payment obligations. The purpose of liquidity risk management is to ensure the availability of liquid assets sufficient to meet potential obligations.

The Group manages its liquidity risk in accordance with the Group's Liquidity Risk Management Policy. Liquidity risk is assessed and decisions are made by ALCO. The decisions of ALCO are approved by the Bank's Management Board. ALCO sets the acceptable liquidity risk level, the Group's internal limit system and defines instruments for the management of liquidity risk, as well as monitors the compliance with the set limits. Liquidity risk management is the responsibility of the Treasury Sector, while risk measuring, monitoring and reporting is within the responsibility of the Risk and Compliance Sector.

Liquidity risk is assessed and related decisions are made by the Bank's Management Board. Daily liquidity management, as well as liquidity risk measurement, management and reporting is ensured by the Treasury Sector in collaboration with Finance department. Liquidity risk management in the Group is coordinated by the Risk and Compliance Sector. However the main source of liquidity is the funding provided by the State Treasury. By persistently improving the liquidity situation, the Bank as of July 2009 is in compliance with liquidity ratio requirements. Also starting from period ended in August 2009 the Bank meets mandatory reserve requirements in the Bank of Latvia.

Currency risk

Currency risk is a risk of loss arising from fluctuations in currency exchange rates.

Currency risk management in the Group is carried out in accordance with the Group's Currency Risk Management Policy. Currency risk is assessed and decisions on limits set are made by the Financial Market and Counterparty Committee (FMCC). The decisions of FMCC are approved by the Bank's Management Board. FMCC defines the acceptable currency risk level and the Group's internal limit system, as well as monitors compliance with these limits.

Day-to-day currency risk management is the responsibility of Treasury Sector, while risk monitoring and reporting is the responsibility of Risk and Compliance Sector. The Group has set a limit for open currency positions in each currency at 10% of its equity, and the limit for the total open currency position at 20% of its equity. The limits are equal to the requirements by Latvian legislation. To assess currency risk, the Group also uses scenario analysis.

As at the date of approval of this report, due to limited access to currency risk mitigation instruments, the Bank and Group was not able to comply with the limits in relation to certain open currency positions. The full compliance will be restored, once the Bank is able to operate as before in the financial markets and re-opens the limits with currency dealers.

Operational risk

The Group defines operational risk as the risk of losses resulting from processes that are deficient or non-compliant with requirements of external and internal regulations, losses resulting from actions of employees and system malfunctioning, as well as losses resulting from actions of third parties or from other external conditions, including legal risk (risk of penalty fees, sanctions applied by external institutions, losses resulting from litigation and other similar events), but excluding strategic risk and reputation risk. The Group further divides operational risk into the following categories: personnel risk, process risk, IT and systems risk, external risk.

The Group does not accept operational risks with potential impact exceeding 10% of the Group’s net annual revenues, as well as unmanageable risks or risks with unquantifiable impact, irrespective of the financial gains this could bring (i.e., the Group does not perform business activities incurring such operational risks).

The Group applies following approaches for operational risk management:

- Self-assessment of operational risk – the business-owners of the products and processes perform identification and evaluation of potential operational risk events, assessment of the existing control systems and the analysis of the required risk mitigation measures using self-assessment questionnaires and brainstorming sessions with the experts of the respective process;
- Defining operational risk indicators – use of statistical, financial and other indicators that reflect the level of various operational risk types and its changes within the Group;
- Defining the limits of the acceptable losses;
- Operational risk measurement by recording and analysing operational risk events, the extent of the respective damage incurred, causes and other related information (data base of operational risk losses and incidents);
- “Four-eye-principle” and segregation of duties;
- Business continuity planning;
- Risk assessment within product development;
- Insurance;
- Investments in appropriate data processing and information protection technologies.