MORTGAGE AND LAND BANK OF LATVIA

Interim Condensed Consolidated and Bank Financial Statements for the 6 months period ended 30 June 2011 in accordance with International Accounting Standard 34 as adopted by European Union

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REPORT OF THE SUPERVISORY COUNCIL AND THE BOARD OF DIRECTORS

During the first six months of 2011 the national economy of Latvia has experienced a moderate recovery – the exporting branches have returned to pre-crisis levels and maintained external trade stable. Also domestic consumption branches witnessed stabilisation of situation. The profit markers of Latvian companies keep improving, however more rapid revival of business activities was hindered by inflation (in June, 2011 – 4.8%) and debts piled up over the past years. The unemployment rate remains high (at the end of June – 12.6%).

The beginning of 2011 was marked with a positive assessment of the economic development potential of Latvia acknowledged also by international rating agencies. *Having upgraded Latvia's sovereign rating by one notch to BBB*- the *Fitch Ratings returned Latvia's sovereign rating to investment grade as well as established a positive rating outlook. The Standard & Poor's Rating Services* upgraded the outlook on Latvia's sovereign rating to positive from stable. On June 6 the *Moody's Investors Service Ltd* uplifted outlook on Latvia's sovereign rating to positive from stable retaining the sovereign rating at previous "Baa3". In their report *Moody's Investors Service Ltd* explained that outlook on Latvia's sovereign rating was changed to positive from stable based on recovery of the country's economy, good medium-term growth forecasts and consolidation of the budget. On June 27 the *Moody's* confirmed the rating of Mortgage Bank's long-term foreign currency deposits at previous Baa3 level. The *Moody's* based retaining of the previous rating for the long-term foreign currency deposits on the fact that Mortgage Bank was a state-owned bank having significant role in channelling the loan funds to small and medium enterprises. The Mortgage Bank is assigned the following ratings:

- long-term foreign currency deposits – *Baa3*,
- short-term foreign currency deposits – *P3*,
- financial strength rating – *E+*,
- mortgage bonds' rating – *Baa2*,

all of which are investment grade ratings.

In the first half-year of 2011, proceeding with transformation of the Bank in line with the transformation concept approved by Cabinet of Ministers, the Mortgage Bank continued active absorption of the current state aid programmes and phasing out of its commercial loans' portfolio. As regards commercial activities the Bank has ceased lending to new customers. Commercial loans are granted only to the existing customers in proportion to the already granted amounts and for restructuring of the loans of the existing commercial customers.

During the first half-year of 2011 the gross assets of the Mortgage Bank decreased by 59.3 mln lats or 7% reaching 748.9 mln lats at the end of June. Within the first 6 months of 2011 the gross loans' portfolio of the Mortgage Bank shrunk by 5% resulting in 568.7 mln lats composed of development loans' portfolio of 236.3 mln lats (42 % of the portfolio) and commercial loans' portfolio of 332.4 mln lats (58% of the portfolio). The volume of deposits has increased by 19.4 mln lats or 5.3 % reaching 382.9 mln lats within the reporting period. In the first half-year the Bank's net profit was 3.1 mln lats. As at the end of June the capital adequacy ratio was 16.3%. On March 16, 2011 the Mortgage Bank, using its own funds only, made an early repayment of 55.5 mln euros (39 mln lats) of syndicated loans granted by „Raiffeisen Bank International AG" and „Sumitomo Mitsui Banking Corporation" still maintaining high liquidity (liquidity ratio 66.4 %). Having repaid these loans the Mortgage Bank has completely settled its obligations towards foreign syndicated lenders.

At the end of June, 2011 the Mortgage Bank, commissioned by government, was implementing the following aid programmes supporting elected groups of entrepreneurs and population:

- Programme for Improvement of Competitiveness of Businesses or *Venture loans*;
- Support to Self-employment and Business Start-ups or *Start-ups programme*;
- Loans for Promotion of Development of Micro, Small and Medium Enterprises and Agricultural Co-operative Unions *or SME Growth loans*;
- Working Capital Loans for Farmers;
- Credit Fund for agriculture, development of countryside and fisheries.

REPORT OF THE SUPERVISORY COUNCIL AND THE BOARD OF DIRECTORS (continued)

Programme for Improvement of Competitiveness of Businesses
As at June 30, 2011 there were loans for 151.3 mln lats granted within the programme of which 63.1 mln lats – from the resources of the Credit Fund.
Start –up programme „Support to Self-employment and Business Start-ups"
As at June 30, 2011, 1816 applicants had applied for consultations and training, 996 participants of the programme had completed their training, 871 business plans were submitted to the Bank of which 788 were examined at credit committee and 465 projects were supported with finances the sum total of the loans being 5.8 mln lats.
SME Growth Programme
In 2010 the Bank started to disburse SME growth loans in accordance with the aid programme „Loans for Promotion of Development of Micro, Small and Medium Enterprises and Agricultural Co-operative Unions". As at June 30, 2011 there were 14.7 mln lats worth SME loans granted.
Working Capital Loans for Farmers
In 2010 the Mortgage Bank started to grant working capital loans to farmers. The loans are granted in line with the Cabinet of Ministers Regulation No 403 of April 27, 2010 "Procedure for Granting State Aid for Acquisition of Working Capital for Production of Agricultural Produce". The total funding of the programme was increased to 18 mln lats to be released from the State Treasury as loans to Mortgage Bank. As at June 30, 2011 the programme had granted 399 loans for the total of 11.7 mln lats. The funding of the programme is consumed and new loans are granted from reflows.
Credit Fund
On 20 July 2010, the Cabinet of Ministers Regulation No 664 "Procedure of Administration and Monitoring the State and European Union Support to Agriculture, Rural Territories and Development of Fish Farming, by Establishing a Credit Fund" (hereinafter – Credit Fund) was approved. The Credit Fund grants loans to finance projects approved by the Rural Support Service. The loans are granted to investments into agricultural enterprises – construction, procurement of stationary machinery and its equipment, procurement of building materials and development of detail design. As at June 30, 2011 the Mortgage Bank had approved 11 projects for the sum total of 6.3 mln lats.

During the second half-year of 2011 within the framework of Latvia – Switzerland co-operation programme the Mortgage Bank will launch „Micro Lending Programme 2" with the co-financing from the Swiss government. Micro enterprises and business start-ups will be able to apply for a loan up to LVL 10 thsd before actual establishment of the micro enterprise. A grant of 750 lats credited towards repayment of the loan will be available to those micro enterprises that have successfully implemented their business projects, spent the funds on the purpose of the business project and complied with other provisions of the loan agreement.

At the end of the first-half year the Mortgage Bank serviced its customers in 10 branches and 24 sub-branches situated in Riga and other cities of Latvia.

On April 12, 2011 the Cabinet of Ministers reviewed informative report drafted by the Ministry of Finance (MoF) on the transformation plan of the state-owned JSC "Mortgage and Land Bank of Latvia" and decided to forward the transformation plan elaborated jointly by MoF and consultant "SEB Enskilda" attracted by Bank to the European Commission

The consultant „SEB Enskilda" was approved for drafting and pursuit of the implementation strategy of the transformation scenario of the Bank.

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Andžs Ūbelis	Jēkabs Krieviņš
Deputy Chairman of the Council	Deputy Chairman of the Board

Riga, 10 August 2011

THE SUPERVISORY COUNCIL AND THE BOARD OF DIRECTORS OF THE BANK

As at 30 June 2011 and as at the date of signing the accounts:

Supervisory Council (at 30 June 2011)

Baiba Bāne	Chairman of the Council
Andžs Ūbelis	Deputy Chairman of the Council
Jānis Pone	Member of the Council

Board of Directors (at 30 June 2011)

Rolands Paņko	Chairman of the Board
Jēkabs Krieviņš	Deputy Chairman of the Board
Jānis Bērziņš	Member of the Board
Baiba Brigmane	Member of the Board
Gints Āboltiņš	Member of the Board

STATEMENT OF RESPONSIBILITY OF THE SUPERVISORY COUNCIL AND THE BOARD OF DIRECTORS

Riga 12 August 2011

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

The financial statements on pages 8 to 27 are prepared in accordance with the source documents and present fairly the financial position of the Bank as at 30 June 2011 and the results of its operations and cash flows for the 6 months period ended 30 June 2011.

The financial statements are prepared in accordance with International Accounting Standard (IAS) 34, Interim Financial Reporting, as adopted by the EU, on a going concern basis. Appropriate accounting policies have been applied on a consistent basis. Prudent and reasonable judgments and estimates have been made by the Management in the preparation of the financial statements.

The Management of the Bank is responsible for the maintenance of proper accounting records, the safeguarding of the Bank's assets and the prevention and detection of fraud and other irregularities in the Bank. They are also responsible for operating the Bank in compliance with the Law on Credit Institutions, regulations of the Financial and Capital Market Commission, Bank of Latvia and other legislation of the Republic of Latvia applicable for credit institutions.

On behalf of the management,

Andžs Ūbelis	Jēkabs Krieviņš
Deputy Chairman of the Council	Deputy Chairman of the Board

INDEPENDENT AUDITORS' REPORT

To the shareholder of VAS Latvijas Hipotēku un zemes banka

Report on the Financial Statements

We have audited the interim condensed consolidated financial statements of VAS Latvijas Hipotēku un Zemes banka and its subsidiaries (hereinafter – the Group) and the accompanying interim condensed financial statements of VAS Latvijas Hipotēku un Zemes banka (hereinafter - the Bank), which are set out on pages 8 through 27 and which comprise the financial position as at 30 June 2011, the statement of comprehensive income, changes in equity and cash flows for the six month period ended 30 June 2011, and explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the International Financial Reporting Standards as adopted by the European Union and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the interim condensed financial statements of the Group and the Bank have been prepared, in all material respects, in accordance with International Accounting Standard 34, as adopted by the EU.

Emphasis of matter

We draw attention to Note 1 in the financial statements, which discusses the uncertainties in the light of the ongoing transformation of the Bank, because the government has not yet taken decision on approval of detailed Bank's transformation plan and sales strategy of commercial segment. Our opinion is not qualified in respect of this matter.

SIA Ernst & Young Baltic
Licence No. 17

Diāna Krišjāne
Chairperson of the Board

Mārtiņš Valters
Latvian Certified Auditor
Certificate No. 185

Riga,
12 August 2011

STATEMENT OF COMPREHENSIVE INCOME (all amounts in thousands of Euro)

	Notes	6 months to 30 June 2011		6 months to 30 June 2010	
		Group	**Bank**	**Group**	**Bank**
Interest income	4	30,337	29,795	31,103	30,343
Interest expense	5	(12,722)	(12,723)	(22,870)	(22,883)
Net interest income		**17,615**	**17,072**	**8,233**	**7,460**
Fee and commission income		2,790	2,178	2,655	2,339
Fee and commission expense		(559)	(630)	(667)	(669)
Net fee and commission income		**2,231**	**1,548**	**1,988**	**1,670**
Net trading income		676	684	1 754	1 705
Other operating income		2 343	649	2 840	1 623
		22 865	**19 953**	**14 815**	**12 458**
Personnel expenses		(6,288)	(5,344)	(6,367)	(5,680)
Administrative expenses		(6,009)	(3,792)	(4,693)	(4,089)
Depreciation and amortisation		(1,229)	(1,117)	(1,382)	(1,261)
Impairment expenses	6	(4,797)	(5,336)	(58,295)	(57,310)
Profit/ (loss) before income tax		**4 542**	**4 364**	**(55 922)**	**(55 882)**
Income tax expense	7	(14)	0	(30)	0
Profit / (loss) for the period		**4,528**	**4,364**	**(55,952)**	**(55,882)**
Net gain from investment securities available-for-sale		250	250	3,152	3,152
Total comprehensive profit / (loss) for the period		**4,778**	**4,614**	**(52,800)**	**(52,730)**
Profit / (loss) for the period attributable to:					
Equity holders of the Bank		4,505	-	(55,960)	-
Non-controlling interest		24	-	9	-
Total comprehensive profit / (loss) for the period attributable to:					
Equity holders of the Bank		4,755	-	(52,808)	-
Non-controlling interest		24	-	9	-

The notes on pages 13 to 27 are an integral part of these financial statements.

These financial statements on pages 8 to 27 have been accepted by the Board of Directors on 10 August 2011 and accepted by the Supervisory Council on 12 August 2011 and are signed by:

Andžs Ūbelis
Deputy Chairman of the Council

Jēkabs Krieviņš
Deputy Chairman of the Board

STATEMENT OF FINANCIAL POSITION (all amounts in thousands of Euro)

	Notes	30/06/11		31/12/10	
Assets		**Group**	**Bank**	**Group**	**Bank**
Cash and balances with Central Bank		81,821	81,821	97,007	97,007
Due from credit institutions		36,512	30,179	29,559	23,751
Derivative financial instruments		1,015	1,015	1,227	1,227
Trading securities	8	2,972	2,686	3,660	3,378
Investment securities – available for sale	8	75,805	84,284	101,741	110,650
Investment securities – held to maturity	8	25,639	25,639	35,023	35,023
Loans to customers	9	675,332	671,472	699,684	669,510
Deferred expenses and accrued income		1,508	1,976	1,682	2,915
Investment properties	11	21,784	1,649	15,045	1,649
Property and equipment		8,796	8,099	9,367	8,643
Intangible assets		2,278	1,742	2,577	2,059
Investments in subsidiaries and associated undertakings		0	1,164	-	1,164
Other assets		6,494	3,744	8,052	3,267
Assets held for sale	10	-	25,484	-	44,031
Total assets		**939,956**	**940,954**	**1,004,624**	**1,004,274**
Liabilities					
Due to credit institutions	12	154,641	154,641	238,717	238,717
Derivative financial instruments		81	84	18	18
Due to customers	13	542,150	544,934	513,889	517,387
Issued debt securities	14	34,469	35,365	46,370	47,020
Deferred income and accrued expenses		2,288	1,784	2,399	1,742
Provisions for off-balance sheet commitments		299	299	1,500	1,500
Current income tax liabilities		0	0	57	-
Deferred tax liabilities		31	0	14	-
Other liabilities		34,991	35,930	35,434	34,587
Subordinated liabilities		44,236	44,236	44,236	44,236
Total liabilities		**813,186**	**817,273**	**882,634**	**885,207**
Shareholder's equity					
Share capital		272,624	272,624	272,624	272,624
Reserve capital		3,591	2,935	3,591	2,935
Revaluation reserve on available for sale investments		297	297	47	47
Accumulated loss		(150,276)	(152,175)	(154,781)	(156,539)
Total shareholder's equity attributable to shareholders of the Bank		**126,236**	**123,681**	**121,481**	**119,067**
Non-controlling interest		534	0	509	-
Total shareholder's equity		**126,770**	**123,681**	**121,990**	**119,067**
Total liabilities and shareholder's equity		**939,956**	**940,954**	**1,004,624**	**1,004,274**

The notes on pages 13 to 27 are an integral part of these financial statements.

These financial statements on pages 8 to 27 have been accepted by the Board of Directors on 10 August 2011 and accepted by the Supervisory Council on 12 August 2011 and are signed by:

Andžs Ūbelis	Jēkabs Krieviņš
Deputy Chairman of the Council	Deputy Chairman of the Board

CONSOLIDATED STATEMENT OF CHANGES IN THE GROUP'S EQUITY
(all amounts in thousands of Euro)

	Attributable to equity holders					
	Share Capital	**Reserve capital**	**Revaluation gain/(loss) on available for sale investments**	**Retained earnings**	**Minority interest**	**Total equity**
Balance as at 31 December 2009	**172,624**	**3,591**	**(4,317)**	**(60,422)**	**57**	**111,533**
Loss for the period	-	-	-	(55,960)	7	**(55,953)**
Other comprehensive expenses	-	-	3,152	-	-	**3,152**
Total comprehensive (loss) / profit for the period	**-**	**-**	**3,152**	**(55,960)**	**7**	**(52,801)**
Shareholders cash contribution	100,000	-	-	-	**-**	**100,000**
Balance as at 30 June 2010	**272,624**	**3,591**	**(1,165)**	**(116,382)**	**64**	**158,732**
Balance as at 31 December 2010	**272,624**	**3,591**	**47**	**(154,781)**	**510**	**121,991**
Profit for the period	-	-	-	4,505	24	**4,529**
Other comprehensive income	-	-	250	-	-	**250**
Total comprehensive profit for the period	**-**	**-**	**250**	**4,505**	**24**	**4,779**
Balance as at 30 June 2011	**272,624**	**3,591**	**297**	**(150,276)**	**534**	**126,770**

The notes on pages 13 to 27 are an integral part of these financial statements.

STATEMENT OF CHANGES IN THE BANK'S SHAREHOLDER'S EQUITY

(all amounts in thousands of Euro)

	Share Capital	Reserve capital	Revaluation gain/ (loss) on available for sale investments	Retained earnings	Total equity
Balance as at 31 December 2009	**172,624**	**2,935**	**(4,317)**	**(59,897)**	**111,345**
Loss for the period		-	-	-	(55,882)
Other comprehensive expenses		-	-	3,152	-
Total comprehensive (loss) / profit for the period		**-**	**-**	**3,152**	**(55,882)**
Shareholders cash contribution	100,000	-	-	-	**100,000**
Balance as at 30 June 2010	**272,624**	**2,935**	**(1,165)**	**(115,779)**	**158,615**
Balance as at 31 December 2010	**272,624**	**2,935**	**47**	**(156,539)**	**119,067**
Profit for the period	-	-	-	4,364	**4,364**
Other comprehensive income	-	-	250	-	**250**
Total comprehensive profit for the period	**-**	**-**	**250**	**4,364**	**4,614**
Balance as at 30 June 2011	**272,624**	**2,935**	**297**	**(152,175)**	**123,681**

The notes on pages 13 to 27 are an integral part of these financial statements.

STATEMENT OF CASH FLOWS (all amounts in thousands of Euro)

	6 months to 30 June 2011		6 months to 30 June 2010	
	Group	**Bank**	**Group**	**Bank**
Cash flows from operating activities				
Profit / (loss) before taxation	4,542	4,364	(55,922)	(55,882)
Depreciation and amortisation	1,229	1,117	1,382	1,261
Increase in provision for impairment losses	4,797	5,336	58,295	57,310
(Profit) / loss from sale of property and equipment	6	7	(211)	(1)
Increase/ (decrease) in deferred income and accrued expenses	(151)	14	303	120
(Increase)/ decrease in deferred expenses and accrued income	174	939	(546)	(522)
(Increase) / decrease in other assets	(5,505)	(1,553)	(4,436)	970
(Decrease)/ increase in other liabilities	(1,579)	206	350	623
(Decrease)/ increase in cash and cash equivalents from operating activities before changes in assets and liabilities	**3,513**	**10,430**	**(785)**	**3,879**
Decrease in balances due from credit institutions	267	267	4,466	4,466
Decrease in loans to customers	18,218	11,113	48,560	44,143
Decrease in trading securities	687	692	4,310	4,178
(Decrease) / increase in balances due to credit institutions	(28,551)	(28,551)	63,564	63,564
Increase in balances due to customers	28,261	27,547	2,178	3,061
Decrease in debt securities issued	(11,901)	(11,655)	(2,119)	(2,957)
Cash and cash equivalents from operating activities	**10,494**	**9,843**	**120,174**	**120,334**
Corporate income tax paid	**(14)**	**-**	**(21)**	**-**
Cash flows from investing activities				
Purchase of investment securities	(21,320)	(21,312)	(139,496)	(139,496)
Sale of investment securities	58,719	58,719	138,302	138,302
Purchases of property and equipment	(403)	(263)	(273)	(223)
Proceeds from property and equipment disposal	37	0	239	14
Cash and cash equivalents from/ (used in) investing activities	**37,033**	**37,144**	**(1,228)**	**(1,403)**
Cash flows from financing activities				
Repayment of syndicated loan	(55,542)	(55,542)	(69,863)	(69,863)
Cash and cash equivalents generated from financing activities	**(55,542)**	**(55,542)**	**(69,863)**	**(69,863)**
Increase / (decrease) in cash and cash equivalents	(8,029)	(8,554)	49,054	49,068
Cash and cash equivalents at the beginning of the year	125,810	120,002	158,027	157,835
Cash and cash equivalents at the end of the year	**117,781**	**111,448**	**207,081**	**206,903**
Cash flow from interest received	25,381	25,852	28,796	27,974
Cash flow from interest paid	15,903	15,905	21,613	21,626

The notes on pages 13 to 27 are an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

1 GENERAL INFORMATION

The Mortgage and Land Bank of Latvia was established as a state-owned commercial bank on 19 March 1993 by the Government of Latvia based on the Decree No 140 adopted by the Cabinet of Ministers. The Bank was registered with the Register of Enterprises of the Republic of Latvia on 3 June 1993. According to the Commercial Law the Bank was registered in the Commercial Register on 14 July 2004.

The operations of the Bank are regulated by the law On Credit Institutions and other effective laws of the Republic of Latvia, the Statutes of the Bank, the instructions of the Bank of Latvia and Financial and Capital Market Commission, as well as the decrees and regulations of the Cabinet of Ministers of the Republic of Latvia. The Bank is under the jurisdiction of the Ministry of Finance of the Republic of Latvia that represents the interests of the shareholder on behalf of the Cabinet of Ministers and holds 100% of the Bank’s shares.

The principal activities of the Bank have been dividend by commercial activities, where Bank provides universal bank’s services, and state support programs, where Bank issues loans under state and European Union programs.

On 3 December 2009, the concept for Transformation of the State-owned JSC Mortgage and Land Bank of Latvia into a Development Bank was approved by Order No 820 issued by the Cabinet of the Republic of Latvia. The concept stipulates that the Mortgage Bank be gradually transformed into a development bank, phasing out commercial functions to completely refuse from them by 31 December 2013 at the latest. The Mortgage Bank will be gradually reducing its commercial loan portfolio and the portfolio balance outstanding at the end of the transition period will be realised or transferred to another financial institution.

In April 2010 the Bank’s shareholder increased its equity capital by 70.28 mln lats. The shareholder has notified the European Commission (EC) about increase of the equity capital. The management of the Bank anticipates that EC will pass a decision on the issue upon analysis of the Bank’s transformation plan and sale strategy of the commercial component (see below) ensuing from the transformation plan. Hence no approval has been received as at the moment of signing this report. Should the approval be denied, the Bank’s shareholder would have to recover the provided support. In these financial statements the influx of capital has been recorded as equity capital and included in the capital adequacy calculation.

On April 12, 2011 the Cabinet of Ministers received the Mortgage Bank’s transformation plan drafted by consultant - „SEB Enskilda”. The transformation plan stipulates sale of the Bank’s commercial assets not related to the functions of development bank. Therefore it was decided to send the transformation plan for review to EC. In May 2011 the Republic of Latvia concluded a memorandum of understanding with the European Union and signed a letter of intent with the International Monetary Fund that among other commitments highlighted the state’s resolution to attract a consultant for drafting of the sale strategy of the Mortgage Bank’s commercial component and forward the said strategy to EC as soon as it was reviewed by Cabinet of Ministers so that it could be implemented during year 2011. On June 15, 2011 the Mortgage Bank’s shareholder and Bank concluded an agreement with the consultant „SEB Enskilda” on drafting and implementing of the sale strategy of the Bank’s commercial assets. As stipulated by agreement the consultant must also define the commercial assets to be sold what causes uncertainty as to exactly which assets of the Bank might be sold. Once the assets’ sale strategy is drafted, the Cabinet of Ministers will have to decide on its implementation and formally submit the strategy to EC to enable the consultant to organize the sale process. Since at the moment of approval of the current financial statements no such decisions were passed, detailed scenario for implementation of the Bank’s transformation process and its timetable remain uncertain. For this reason the financial statements cannot classify the commercial component’s assets that might be sold, as estimated by Bank’s management, according to IFRS 5 „Non-current assets held for sale and discontinued operations”.

NOTES TO THE FINANCIAL STATEMENTS

1 GENERAL INFORMATION (continued)

In line with the consultant's initial estimate made during drafting of the transformation plan, there is a possibility that the value of the commercial component's assets to be sold is lower than their balance value recorded while the transformation plan is being drafted i.e. at the end of 2010. The aforementioned estimate was based on the fact that on similar occasions in Europe where the bank's assets were sold to third parties, there were discounts applied to the fair value of the assets. However, in view of the uncertainties with regard to the transformation plan and development of the sale strategy, the management of the Bank has not been able to assess the potential impact of the draft transformation plan, including impact of the approval of capital increase, on the future activities of the Bank, maturity structure and value of the assets and liabilities and capital adequacy that might occur as a result of the elaboration and implementation of the sale strategy of the commercial component. The Cabinet of Ministers of the Republic of Latvia is to decide on the transformation plan and strategy for divesting of the commercial component upon approval of this report.

These interim financial statements on pages 8 to 27 have been accepted by the Board of Directors on 10 August 2011 and accepted by the Supervisory Council on 12 August 2011. In accordance with the Commercial Law of the Republic of Latvia, the shareholders' meeting has the right to make decision on approval of the financial statements.

2 ACCOUNTING POLICIES

(1) Basis of preparation

These interim condensed consolidated financial statements are prepared in accordance with IAS 34 "Interim Financial Reporting" as adopted by EU. These interim financial statements should be read in conjunction with the 2010 annual financial statements which have been prepared in accordance with IFRSs.

The financial statements are prepared under the historical cost convention as modified by the fair valuation of financial assets held as available-for-sale, trading securities, derivative financial instruments and investment properties.

The preparation of financial statements in accordance with International Financial Reporting Standards requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on Management's best knowledge of current events and actions, actual results ultimately may differ from those estimates.

In order to improve financial statement presentation, the Group has changed presentation of several statement of comprehensive income and financial position classifications, as well as made reclassifications in prior period balances. Key changes in the statement of income relates to reclassifying penalty income from caption Other operating income to Interest income in amount of 1,436 thousand LVL and recovery of loans written off in previous periods from caption Other operating income to Impairment expenses, net in amount of 930 thousand LVL.

(2) Adoption of New or Revised Standards and Interpretations

The accounting policies adopted are consistent with those of the previous financial year except as follows:

The Group has adopted the following new and amended IFRS and IFRIC interpretations as of 1 January 2011:

- IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments
- IFRIC 14 Prepayments of a Minimum Funding Requirement (Amended)
- IAS 32 Classification on Rights Issues (Amended)
- IAS 24 Related Party Disclosures (Revised)
- Improvements to IFRSs (May 2010)

NOTES TO THE FINANCIAL STATEMENTS

2 ACCOUNTING POLICIES (continued)

(2) Adoption of New or Revised Standards and Interpretations (continued)

When the adoption of the standard or interpretation is deemed to have an impact on the financial statements or performance of the Group, its impact is described below:

In May 2010 the IASB issued its third omnibus of amendments to its standards, primarily with a view to removing inconsistencies and clarifying wording.

IFRS 3 Business Combinations

IFRS 7 Financial Instruments: Disclosures
This improvement gives clarifications of disclosures required by IFRS 7 and emphasises the interaction between quantitative and qualitative disclosures and the nature and extent of risks associated with financial instruments.

IAS 1 Presentation of Financial Statements

IAS 27 Consolidated and Separate Financial Statements

IAS 34 Interim Financial Reporting
This improvement requires additional disclosures for fair values and changes in classification of financial assets, as well as changes to contingent assets and liabilities in interim condensed financial statements.

IFRIC 13 Customer Loyalty Programmes

The Group has not early adopted any other standard, interpretation or amendment that has been issued byt is not yet effective.

3 RISK MANAGEMENT

The Group and the Bank Risk Management Policy has not changed in 2011.

The following table presents the key indicators of the Bank's risk management:

	30/06/11 Bank	**31/12/10 Bank**
Credit Risk		
Ratio of large exposure concentration and own funds (< 400%)	43.3%	33.6%
Ratio of single client’s (related clients’ group) large exposure and own funds (< 25%)	24.0%	21.2%
Ratio of risk exposures with persons related to the Bank and own funds (< 15%)	1.1%	1.0%
Proportion of risk concentration in a single economic sector in the Bank’s credit portfolio and own funds	135.4%	131.9%
Proportion of the Bank’s total claims to non-residents	7.5%	7.3%
Liquidity Risk		
Liquidity ratio (> 30%)	66.4%	84.4%
Capital Adequacy		
Capital adequacy ratio (> 8%)	16.3%	16.7%
Internal capital adequacy ratio	11.4%	11.7%

NOTES TO THE FINANCIAL STATEMENTS

4 INTEREST INCOME

	6 months to 30 June 2011		6 months to 30 June 2010	
	Group	**Bank**	**Group**	**Bank**
Interest income:				
- interest on balances due from credit institutions	156	126	472	471
- interest on loans to customers	19,747	19,396	18,218	17,688
Including on impaired loans (see Note 9)	*2,717*	*2,182*	-	-
- interest on securities	1,418	1,418	3,169	3,166
	21,321	**20,940**	**21,859**	**21,325**

5 INTEREST EXPENSE

	6 months to 30 June 2011		6 months to 30 June 2010	
	Group	**Bank**	**Group**	**Bank**
Interest expense:				
- interest on balances due to credit institutions	4,660	4,660	7,708	7,708
- interest on current and deposit accounts	2,584	2,584	6,402	6,402
- interest on subordinated liabilities	894	894	894	894
- interest on mortgage bonds issued	442	443	736	745
- payments to the deposit guarantee fund	326	326	295	295
- other interest expense	35	35	38	38
	8,941	**8,942**	**16,073**	**16,082**

6 PROVISION FOR IMPAIRMENT LOSSES

	6 months to 30 June 2011		6 months to 30 June 2010	
	Group	**Bank**	**Group**	**Bank**
Impairment expenses on:				
- loans	6,834	6,930	48,984	48,849
- other assets	183	183	973	221
- securities	12	12	21	21
- investments in subsidiaries	-	-	3	3
- due from credit institutions	-	-	20	20
- provisions for off balance sheet liabilities	1,631	1,631	848	848
	8,660	**8,756**	**50,849**	**49,962**
Release of impairment expenses on:				
- loans	(2,987)	(2,704)	(8,083)	(7,888)
- other assets	-	-	(13)	(13)
- securities	(1)	(1)	(736)	(736)
- due from credit institutions	(33)	(33)		
- provisions for off balance sheet liabilities	(1,094)	(1,094)	(117)	(117)
	(4,115)	**(3,832)**	**(8,949)**	**(8,754)**
Recovery of loans written off in the previous periods	**(1,174)**	**(1,174)**	**(930)**	**(930)**
Total impairment expenses, net	**3,371**	**3,750**	**40,970**	**40,278**

NOTES TO THE FINANCIAL STATEMENTS

7 CORPORATE INCOME TAX

As at 31 December 2010 the Bank had accumulated tax losses of LVL 134,473 thousand, which it can carry forward and utilise in future years. As at 30 June 2011 taxable profit was LVL 3,239 thousand, which has been covered by accumulated tax losses. In accordance with the legislation of the Republic of Latvia tax losses carried forward can be covered in chronological order from taxable income during the following eight years.
Given uncertainties with Bank's transformation, it has resolved not to recognize any deferred tax asset.

8 TRADING AND INVESTMENT SECURITIES

	30/06/11		31/12/10	
	Group	**Bank**	**Group**	**Bank**
Trading securities				
Latvian Treasury bills and government bonds	-	-	509	509
Latvian corporate bonds	111	111	106	106
Investment funds registered in Latvia	1,978	1,777	1,957	1,759
Total trading securities	**2,089**	**1,888**	**2,572**	**2,374**
Securities held to maturity				
OECD government bonds	1,226	1,226	1,293	1,293
Non-OECD government bonds	5,015	5,015	6,057	6,057
OECD corporate bonds	9,206	9,206	10,111	10,111
Non-OECD corporate bonds	2,392	2,392	6,591	6,591
Latvian corporate bonds	3,007	3,007	3,517	3,517
Total securities held to maturity	**20,846**	**20,846**	**27,569**	**27,569**
Provisions for impairment losses on securities	(2,827)	(2,827)	(2,955)	(2,955)
Total net securities held to maturity	**18,019**	**18,019**	**24,614**	**24,614**
Securities available-for-sale				
Latvian Treasury bills and government bonds	48,488	47,831	67,601	66,939
OECD government bonds	359	359	371	371
OECD corporate bonds	523	523	-	-
Non-OECD corporate bonds	302	-	-	-
Investment funds registered in Latvia*	3,604	10,522	3,532	10,455
Total securities available-for-sale	**53,276**	**59,235**	**71,504**	**77,765**
Total net trading and investment securities	**73,384**	**79,142**	**98,690**	**104,753**

*Bank has consolidated certain closed investment funds in the consolidated reports.

The following table shows the division of the Bank's debt securities by rating agency designation (*Moody`s investors Service*) as at 30 June 2011:

	Trading securities	**Investment securities available-for-sale**	**Securities held to maturity**	**Total net**
Aa1 - Aa3	-	359	2,590	2,949
A1 - A3	-	-	3,822	3,822
Baa1 - Baa3	-	48,096	8,122	56,218
Lover than Baa3	-	258	1,433	1,691
Unrated	111	-	2,052	2,163
Total	**111**	**48,713**	**18,019**	**66,843**

NOTES TO THE FINANCIAL STATEMENTS

8 TRADING AND INVESTMENT SECURITIES (continued)

The following table shows the division of the Bank's debt securities by rating agency designation (*Moody`s investors Service*) as at 31 December 2010:

	Trading securities	Investment securities available-for-sale	Securities held to maturity	Total net
Aa1 - Aa3	-	371	3,320	3,691
A1 - A3	-	-	4,611	4,611
Baa1 - Baa3	509	66,939	12,034	79,482
Lover than Baa3	106	-	2,050	2,156
Unrated	-	-	2,599	2,599
Total	**615**	**67,310**	**24,614**	**92,539**

As at 30 June 2011 fair value of securities held to maturity was LVL 17,811 thousand (as at 31 December 2010: LVL 23,809 thousand).

All securities are quoted on stock exchange. The average yield on investment securities as at 30 June 2011 was 3.7% (2010: 3.5%).

9 LOANS TO CUSTOMERS

Loans by type of borrower:

	30/06/11		31/12/10	
	Group	**Bank**	**Group**	**Bank**
Private companies	395,202	339,499	402,026	328,597
Individuals	167,597	133,560	175,101	142,177
Financial institutions	104	48,606	297	47,582
State owned companies	1,671	1,671	6,543	6,543
Management / personnel	6,242	5,090	6,851	5,634
Local government	1,199	1,061	1,279	1,109
Public and religious institutions	549	481	596	528
Accrued interest on loans	5,746	4,314	4,977	3,324
Total gross loans	**578,310**	**534,282**	**597,670**	**535,494**
Allowance for impairment loss	(103,684)	(62,369)	(105,929)	(64,960)
Total net loans	**474,626**	**471,913**	**491,741**	**470,534**

97.4% from loans issued by the Bank and the Group are loans to residents of Latvia.

Analysis of loans issued by the Bank by type of valuation:

	30/06/11 Bank			31/12/10 Bank		
	Individuals	**Companies**	**Total loans**	**Individuals**	**Companies**	**Total loans**
Individually assessed loans	47,860	320,117	367,977	47,700	310,281	357,981
Collectively assessed loans	91,540	74,765	166,305	100,786	76,727	177,513
Total gross loans	**139,400**	**394,882**	**534,282**	**148,486**	**387,008**	**535,494**
Allowance for impairment loss – individually assessed	(10,435)	(47,105)	(57,540)	(8,663)	(50,843)	(59,506)
Allowance for impairment loss – collectively assessed	(1,146)	(3,683)	(4,829)	(1,502)	(3,952)	(5,454)
Total net loans	**127,819**	**344,094**	**471,913**	**138,321**	**332,213**	**470,534**

NOTES TO THE FINANCIAL STATEMENTS

9 LOANS TO CUSTOMERS (continued)

Analysis of loans issued by the Group by type of valuation:

	30/06/11 Group			31/12/10 Group		
	Individuals	**Companies**	**Total loans**	**Individuals**	**Companies**	**Total loans**
Individually assessed loans	83,044	327,953	410,997	82,019	337,254	419,273
Collectively assessed loans	92,079	75,234	167,313	101,052	77,345	178,397
Total gross loans	**175,123**	**403,187**	**578,310**	**183,071**	**414,599**	**597,670**
Allowance for impairment loss – individually assessed	(22,918)	(75,624)	(98,542)	(19,525)	(80,523)	(100,048)
Allowance for impairment loss – collectively assessed	(1,208)	(3,934)	(5,142)	(1,599)	(4,282)	(5,881)
Total net loans	**150,997**	**323,629**	**474,626**	**161,947**	**329,794**	**491,741**

The following table provides the division of loans and advances to customers by quality (Bank):

	30/06/11 Bank			31/12/10 Bank		
	Individuals	**Companies**	**Total loans**	**Individuals**	**Companies**	**Total loans**
Neither past due nor impaired	95,821	289,748	385,569	106,856	268,597	375,453
Past due but not impaired	21,956	25,757	47,713	21,129	25,804	46,933
Impaired	21,623	79,377	101,000	20,501	92,607	113,108
Total loans	**139,400**	**394,882**	**534,282**	**148,486**	**387,008**	**535,494**
Provisions for impairment losses on loans	(11,581)	(50,788)	(62,369)	(10,165)	(54,795)	(64,960)
Total net loans	**127,819**	**344,094**	**471,913**	**138,321**	**332,213**	**470,534**

The following table provides the division of loans and advances to customers by quality (Group):

	30/06/11 Group			31/12/10 Group		
	Individuals	**Companies**	**Total loans**	**Individuals**	**Companies**	**Total loans**
Neither past due nor impaired	100,456	229,671	330,127	112,411	230,374	342,785
Past due but not impaired	27,022	36,348	63,370	22,424	31,929	54,353
Impaired	47,645	137,168	184,813	48,236	152,296	200,532
Total loans	**175,123**	**403,187**	**578,310**	**183,071**	**414,599**	**597,670**
Provisions for impairment losses on loans	(24,126)	(79,558)	(103,684)	(21,124)	(84,805)	(105,929)
Total net loans	**150,997**	**323,629**	**474,626**	**161,947**	**329,794**	**491,741**

The following table provides the division of loans and advances to customers past due but not impaired:

	30/06/11 Bank			31/12/10 Bank		
	Individuals	**Companies**	**Total loans**	**Individuals**	**Companies**	**Total loans**
Past due up to 30 days	13,485	14,701	28,186	13,800	20,385	34,185
Past due 30-60 days	2,457	2,462	4,919	2,535	2,609	5,144
Past due 60-90 days	1,547	1,328	2,875	961	1,031	1,992
Past due over 90 days	4,467	7,266	11,733	3,833	1,779	5,612
Total loans	**21,956**	**25,757**	**47,713**	**21,129**	**25,804**	**46,933**

NOTES TO THE FINANCIAL STATEMENTS

9 LOANS TO CUSTOMERS (continued)

The following table provides the division of loans and advances to customers past due but not impaired:

	30/06/11 Group			31/12/10 Group		
	Individuals	**Companies**	**Total loans**	**Individuals**	**Companies**	**Total loans**
Past due up to 30 days	14,949	21,236	36,185	14,824	25,939	40,763
Past due 30-60 days	2,538	2,462	5,000	2,535	2,626	5,161
Past due 60-90 days	1,624	1,328	2,952	961	1,031	1,992
Past due over 90 days	7,911	11,322	19,233	4,104	2,333	6,437
Total loans	**27,022**	**36,348**	**63,370**	**22,424**	**31,929**	**54,353**

The following table provides fair values of collaterals of impaired loans:

	30/06/11 Group	30/06/11 Bank	31/12/10 Group	31/12/10 Bank
Impaired loans	177,731	93,918	196,419	108,995
Value of collateral	86,410	45,533	109,714	58,706

The following table provides the division of restructured loans and advances to customers by type of borrower:

	30/06/11 Group	30/06/11 Bank	31/12/10 Group	31/12/10 Bank
Individuals	21,036	18,644	23,712	18,681
Companies	72,454	105,115	64,002	57,990
Total net restructured loans	**93,490**	**123,759**	**87,714**	**76,671**

Analysis of movement in impairment allowance for loans:

	30/06/11 Bank			30/06/10 Bank		
	Individuals	**Companies**	**Total loans**	**Individuals**	**Companies**	**Total loans**
As at beginning of the year	**19,130**	**73,608**	**92,738**	**22,120**	**51,321**	**73,441**
Impairment charge, net	4,081	145	**4,226**	6,554	34,407	**40,961**
Adjustment (foreign exchange fluctuation)	-	-	**-**	35	63	**98**
Accrued interest (Note 4)	(689)	(1,493)	**(2,182)**	-	-	**-**
Write-off of loans	(6,389)	(9,487)	**(15,876)**	(3,434)	(15,975)	**(19,409)**
As at end of the period	**16,133**	**62,773**	**78,906**	**25,275**	**69,816**	**95,091**
impairment for loan	11,581	50,788	62,369	-	-	-
*impairment for asstes held for sale**	4,552	11,985	16,537	-	-	-

* As described in note 10, the Bank has decided to sell certain loans to its subsidiary. As a result these loans are classified as held for sale in financial position and are valued net of impairment charge.

** Written down loan include loans sold to Banks subsidiary during 2011, with impairment allowance at time of write-down of 12 million LVL.

NOTES TO THE FINANCIAL STATEMENTS

9 LOANS TO CUSTOMERS (continued)

Analysis of movement in impairment allowance for loans:

	30/06/11 Group			30/06/10 Group		
	Individuals	**Companies**	**Total loans**	**Individuals**	**Companies**	**Total loans**
As at beginning of the year	**21,124**	**84,805**	**105,929**	**22,299**	**52,136**	**74,435**
Impairment charge, net	4,379	(532)	**3,847**	6,600	34,301	**40,901**
Adjustment (foreign exchange fluctuation)	-	-	**-**	36	63	**99**
Accrued interest (Note 4)	(803)	(1,914)	**(2,717)**	-	-	**-**
Write-off of loans	(574)	(2,801)	**(3,375)**	(3,484)	(16,201)	**(19,685)**
As at end of the period	**24,126**	**79,558**	**103,684**	**25,451**	**70,299**	**95,750**

As at 30 June 2011 fair value of Group's loans was LVL 472,725 thousand (as at 31 December 2010: LVL 490,634 thousand).

The average interest rate for the loan portfolio as at 30 June 2011 was 6.0% per annum (5.9% at 31 December 2010).

10 ASSETS HELD FOR SALE

	30/06/11		31/12/10	
	Group	**Bank**	**Group**	**Bank**
Loans to:				
Private companies	-	21,518	-	33,574
Individuals	-	12,064	-	23,886
Public and religious institutions	-	68	-	68
Accrued interest on loans	-	797	-	1,195
Total gross assets/loans for sale	**-**	**34,447**	**-**	**58,723**
Provisions for impairment losses	-	(16,537)	-	(27,778)
Total net assets/loans for sale	**-**	**17,910**	**-**	**30,945**

Assets held for sale include non-performing loans which Bank has intended to sell to its subsidiary SIA „Hipotēku bankas nekustamā īpašuma aģentūra".

11 INVESTMENT PROPERTIES

	30/06/11		31/12/10	
	Group	**Bank**	**Group**	**Bank**
Carrying amount at 1 January	**10,574**	**1,159**	**1,166**	**1,166**
Acquired	4,502	-	9,523	-
Value adjustment	234	-	(115)	(7)
Carrying amount at 30 June / 31 December	**15,310**	**1,159**	**10,574**	**1,159**

Investment properties represent properties that are held to earn rentals or for capital appreciation. The investment properties comprise properties taken over by the Group that previously had been pledged as collateral.

NOTES TO THE FINANCIAL STATEMENTS

11 INVESTMENT PROPERTIES (continued)

Investment properties are held at fair value based on valuations made by independent valuers who have up-to-date experience in valuing real estate in the respective location and category and who hold an appropriate professional qualification for real estate valuation. The valuations are made on the basis of recent comparative data in the local market and/or on discounted cash flow method. In case discounted cash flow method is used, key assumptions are made about discount rate, yield, occupancy and rent rate increase. Dependant on the location of the investment property, key assumptions on average range between 9-12% for discount rate, 8-10% for yield, 50%-90% for occupancy rate and future rent price increase between 3%-10% per annum.

12 DUE TO CREDIT INSTITUTIONS

	30/06/11		31/12/12	
	Group	**Bank**	**Group**	**Bank**
Due to credit institutions registered in OECD area	99,993	99,993	153,161	153,161
Due to credit institutions registered in Latvia	8,689	8,689	14,610	14,610
	108,682	**108,682**	**167,771**	**167,771**

During the reporting period, the Bank repaid syndicated loans in amount of LVL 39 thousand thus completely extinguishing all the obligations to the syndicated lenders.

The average interest rate for due to credit institutions as at 30 June 2011 was 2.5% (at 31 December 2010: 2.9%).

13 DUE TO CUSTOMERS

	30/06/11		31/12/10	
	Group	**Bank**	**Group**	**Bank**
Individuals	217,959	217,959	227,954	227,954
Financial institutions	63,521	65,019	49,400	51,852
Private companies	49,195	49,654	49,794	49,801
State owned companies	14,858	14,858	9,023	9,023
Public and religious organisations	9,303	9,303	7,329	7,329
Local government	11,175	11,175	7,146	7,146
Central government	12,228	12,228	6,478	6,478
Accrued interest	2,786	2,786	4,039	4,039
Total due to customers	**381,025**	**382,982**	**361,163**	**363,622**

Due to customers analysis by term:

	30/06/11		31/12/10	
	Group	**Bank**	**Group**	**Bank**
On demand	91,451	92,380	83,518	84,928
Term balances	289,574	290,602	277,645	278,694
Total due to customers	**381,025**	**382,982**	**361,163**	**363,622**

99.6% of the deposits with the Bank are the Bank's liabilities to residents of Latvia, the remaining 0.4% of the deposits are liabilities to other countries residents.

The average interest rate for demand deposits at 30 June 2011 was 0.1% (0.1% at 31 December 2010), for term deposits – 3.2% (4.2% at 31 December 2010).

NOTES TO THE FINANCIAL STATEMENTS

14 ISSUED DEBT SECURITIES

The purpose of mortgage bonds issuing was to attract financial resources for refinancing of the long-term mortgage loans.

The average annual interest rate of the issued securities was 3.2% (as at 31 December 2010: 3.8%).

Statement on Mortgage bond coverage as at 30 June 2011

(a) Issued mortgage bonds

ISIN	Security class	Number of mortgage bonds	Face value	Registered volume	Coupon rate, %	Maturity date	Outstanding volume, LVL	Book value LVL
LV0000800100	AH	20,000	100 LVL	2,000,000	7.5%	15.08.2011.	1,150,000	1,182,463
LV0000800217	BA	100,000	100 USD	10,000,000	1.25%*	15.08.2011.	2,257,713	2,268,356
LV0000800340	CA	200,000	100 EUR	20,000,000	1.625**	15.02.2012.	12,285,014	12,360,350
LV0000800142	AL	50,000	100 LVL	5,000,000	6.0%	15.08.2012.	5,000,000	5,111,337
LV0000800159	AM	70,000	100 LVL	7,000,000	5.25%	15.08.2013.	3,862,400	3,932,383
						Total	**24,555,127**	**24,854,889**

* floating coupon rate (6 month LIBOR plus 0.8%) that is revised twice every year on 15 February and 15 August
**floating coupon rate (6 month EURIBOR plus 0.29%) that is revised twice every year on 15 February and 15 August

(b) Structure of Mortgage bond coverage

Mortgage bonds in circulation are secured by assets included in the Mortgage Bond Cover Register which as of 30 June 2011 amounted to LVL 32,854 thousand (as at 31 December 2010: LVL 41,142 thousand). Assets included in the Mortgage Bond Cover Register consisted of mortgage loans (ordinary cover) in the amount of LVL 32,854 thousand (as at 31 December 2010: mortgage loans - LVL 39,634 thousand and substitute cover amounting - LVL 1,508 thousand).

As at 30 June 2011 the amount of assets included in the Mortgage Bond Cover Register exceeds the amount of mortgage bonds in circulation by 26.3% (as at 31 December 2010: 17.1%) of the amount of weighted assets included in the Mortgage Bond Cover Register (minimum statutory requirement: 10%).

All mortgage bonds issued by the Bank are assigned Baa2 rating by Moody's Investors Service. All issued debt securities are quoted on the Official List of the Riga Stock Exchange.

15 CASH AND CASH EQUIVALENTS

	30/06/11		**31/12/10**		**30/06/10**	
	Group	**Bank**	**Group**	**Bank**	**Group**	**Bank**
Cash	10,898	10,898	9,795	9,795	10,304	10,304
Placements with the Bank of Latvia	46,606	46,606	58,382	58,382	112,591	112,591
Placements with other credit institutions	13,829	13,762	12,209	12,137	23,814	23,689
Placements with other credit institutions with remaining maturity up to 3 months	11,566	7,182	8,144	4,134	5,732	5,732
Placements from other credit institutions with remaining maturity up to 3 months	(122)	(122)	(110)	(110)	(6,904)	(6,904)
	82,777	**78,326**	**88,420**	**84,338**	**145,537**	**145,412**

NOTES TO THE FINANCIAL STATEMENTS

16 OFF BALANCE SHEET ITEMS AND CONTINGENT LIABILITIES

	30/06/11		31/12/10	
	Group	**Bank**	**Group**	**Bank**
Contingent liabilities				
outstanding guarantees	16,222	18,824	16,081	18,466
Financial commitments				
unutilised loan facilities	21,083	53,585	23,033	84,631
Other liabilities	350	350	91	91
Total	**37,655**	**72,759**	**39,205**	**103,188**

17 RELATED PARTY TRANSACTIONS

Related parties are defined as shareholder who has significant influence over the Bank, members of the Council, the Board of Directors and the Bank's higher level management, their close relatives and companies in which they have a controlling interest as well as Bank's subsidiaries and companies, in which the Bank is having a significant influence.

The following loans and deposits were held with related parties at 30 June 2011:

	30/06/11		31/12/10	
	Group	**Bank**	**Group**	**Bank**
Loans:				
- Members of the Council and the Board and high level management	880	880	1,052	1,052
- subsidiaries	-	89,105	-	69,449
- other related parties	2,528	2,528	2,775	2,775
Total loans held by related parties	**3,408**	**92,513**	**3,827**	**73,276**
Deposits:				
- Members of the Council and the Board and high level management	366	366	433	433
- subsidiaries	-	907	-	435
- other related parties	206	206	374	374
Total deposits held by related parties	**572**	**1,479**	**807**	**1,242**

The Banka has entered into a guarantee agreement with SIA Hipolīzings for covering lease losses totalling LVL 6,000 thousand. According to the agreement, the Bank has established impairment allowance for doubtful lease receivables. The balance of the above provisions as at 30 June 2011 amounted to LVL 2,018 thousand (31 December 2010: LVL 3,615 thousand). Impairment allowance for other receivables from subsidiaries as at 30 June 2011 amounted to LVL 4,471 thousand (31 December 2010: LVL 2,586 thousand).

In order to maintain specialization, concentration of competence and higher efficiency within the framework of non-performing loans management process, the Bank has made a decision to concentrate the management function of these loans within the subsidiary company of the Bank SIA "Hipotēku bankas nekustamā īpašuma aģentūra" (LLC Real Estate Agency of the Mortgage bank). During the reporting period, the Bank has sold its non-performing loans of LVL 24,757 thousand, book value, to the subsidiary company SIA "Hipotēku bankas nekustamā īpašuma aģentūra" for LVL 24,663 thousands, as a result of which the Bank recognized additional losses of LVL 94 thousands.

NOTES TO THE FINANCIAL STATEMENTS

17 RELATED PARTY TRANSACTIONS (continued)

Bank's income / (expenses) from transactions with related parties:

	6 months to 30 June 2011		6 months to 30 June 2010	
	Group	**Bank**	**Group**	**Bank**
Interest income from loans to related parties	24	2,224	17	964
Interest expenses for deposits held from related parties	(5)	(6)	(30)	(31)
Total income / (expenses), net	**19**	**2,218**	**(13)**	**933**

The average interest rate as at 30 June 2011 on loans issued to related parties was 4.1% per annum (3.9% as at 31 December 2010). The average interest rate as at 30 June 2011 on deposits held for related parties was 0.7% per annum (1.4% as at 31 December 2010).

During the reporting period, the Bank has not entered into any significant transactions with state institutions.

The Group and the Bank have entered into transactions with related parties in ordinary course of business at commercial terms.

18 SEGMENT ANALYSIS

Group's operations are managed based on two operating segments:
Promotional programs: operating segment comprises loans to particular SME's or individuals according to priorities defined by the Government or within the scope of European Union promotional programs.

Commercial services (Bank): operating segment comprises Bank's services to individuals and legal entities, loans to customers, accounts, savings and investments, serving payment cards.

Commercial services (Associated companies): operating segment comprises associated companies' services with real estate, leasing and asset management.

NOTES TO THE FINANCIAL STATEMENTS

18 SEGMENT ANALYSIS (continued)

6 months to 30/06/2011 Group	**Promotional programs**	**Commercial services Bank**	**Commercial services Associated comp.**	**Reconciliation**	**Group**
Revenue form external customers	8 123	13 107	4 174	-	25 404
Inter-segment revenue	1 087	2 866	93	(4 046)	-
Total revenues	**9 210**	**15 973**	**4 267**	**(4 046)**	**25 404**
Net result	**4 208**	**(1 141)**	**(1 562)**	**1 698**	**3 183**

* Inter-segment revenues of LVL 4,046 thousand are reconciled on consolidation

30/06/2011 Group	**Promotional programs**	**Commercial services Bank**	**Commercial services Associated comp.**	**Reconciliation**	**Group**
Reportable segment assets	**201 510**	**490 894**	**97 160**		**660 605**
Segment assets comprise:					
Cash and balances with Central Bank	-	57 504	-	-	57 504
Securities	-	79 142	408	(6 166)	73 384
Due from credit institutions	-	52 308	933	(27 580)	25 661
Loans to customers	200 396	289 427	75 732	(90 929)	474 626
Other assets	1 114	12 513	20 087	(4 284)	29 430
Total assets	**201 510**	**490 894**	**97 160**	**(128 959)**	**660 605**
Reportable segment liabilities and shareholder's equity	**201 510**	**490 894**	**97 160**		**660 605**
Segment liabilities comprise:					
Due to customers	25 983	356 999	-	(1 957)	381 025
Issued debt securities	-	24 855	-	(630)	24 225
Other liabilities	112 280	54 274	92 297	(123 679)	135 172
Subordinated liabilities	-	31 089	-	-	31 089
Shareholders equity to other segments *	63 247	23 677	4 863	(2 693)	89 094
Total liabilities and shareholder's equity	**201 510**	**490 894**	**97 160**	**(128 959)**	**660 605**

* Shareholders equity for promotional programs is calculated as share capital increase performed both in 2009 and 2010, less any accumulated losses and equity allocated to commercial activities. In April 2010 the management has decided to allocate certain amount of equity form promotional programs to commercial bank activities, based on internally calculated regulatory capital requirements for commercial bank. Promotional programs are charging 5 % interest for this capital. As at 30 June 2011 promotional programs had allocated shareholders equity of LVL 45,000 thousand to commercial activities. The charge for 6 months 2010 was LVL 1,063 thousand.

NOTES TO THE FINANCIAL STATEMENTS

18 SEGMENT ANALYSIS (continued)

6 months to 30/06/2010 Group	**Promotional programs**	**Commercial services Bank**	**Commercial services Associated comp.**	**Reconciliation**	**Group**
Revenue form external customers	10 470	14 721	2 693	-	27 884
Inter-segment revenue	887	4 246	272	(5 405)	-
Total revenues	**11 357**	**18 967**	**2 965**	**(5 405)**	**27 884**
Net result	**(15 575)**	**(23 699)**	**(350)**	**322**	**(39 302)**

* Inter-segment revenues of LVL 5,405 thousand are reconciled on consolidation.

31/12/2010 Group	**Promotional programs**	**Commercial services Bank**	**Commercial services Associated comp.**	**Reconciliation**	**Group**
Reportable segment assets	**221 272**	**537 875**	**75 754**		**706 053**
Segment assets comprise:					
Cash and balances with Central Bank	-	68 177	-	-	68 177
Securities	18 220	80 271	425	(226)	98 690
Due from credit institutions	-	76 292	507	(56 025)	20 774
Loans to customers	202 094	299 385	59 857	(69 595)	491 741
Other assets	958	13 750	14 965	(3 002)	26 671
Total assets	**221 272**	**537 875**	**75 754**	**(128 848)**	**706 053**
Reportable segment liabilities and shareholder’s equity	**221 272**	**537 875**	**75 754**		**706 053**
Segment liabilities comprise:					
Due to customers	23,775	337,823	-	(435)	361 163
Issued debt securities	-	32 815	-	(226)	32 589
Other liabilities	133,360	116,601	71 792	(126 276)	195 477
Subordinated liabilities	-	31 089	-	-	31 089
Shareholders equity to other segments	64 137	19 547	3 962	(1 911)	85 735
Total liabilities and shareholder’s equity	**221 272**	**537 875**	**75 754**	**(128 848)**	**706 053**