

**MORTGAGE AND LAND BANK
OF LATVIA**

**Interim Condensed Consolidated and Bank Financial
Statements for the nine months period ended 30 September
2008 (unaudited)**

*Mortgage and Land Bank of Latvia
Interim Condensed Consolidated and Bank Financial Statements
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INCOME STATEMENT

(all amounts in thousands of Lats)

	9 months to 30 September 2008		9 months to 30 September 2007	
	Group	Bank	Group	Bank
Interest income	48,702	46,799	37,230	35,532
Interest expense	(33,309)	(32,720)	(20,835)	(20,757)
Net interest income	15,393	14,079	16,395	14,775
Fee and commission income	3,103	3,023	3,001	3,017
Fee and commission expense	(694)	(685)	(613)	(566)
Net fee and commission income	2,409	2,338	2,388	2,451
Dividend income	13	813	-	500
Net trading income	1,453	1,422	1,608	1,577
Other operating income	3,666	2,438	3,304	2,453
Staff costs	(7,739)	(6,925)	(7,306)	(6,692)
Administrative expenses	(6,739)	(5,787)	(6,021)	(5,471)
Depreciation and amortisation	(1,772)	(1,525)	(1,799)	(1,698)
Provision for impairment losses	(4,536)	(4,096)	(1,950)	(1,705)
Profit before income tax	2,148	2,757	6,619	6,190
Income tax expense	(621)	(567)	(1,198)	(1,059)
Minority interest	5	-	-	-
Net profit for the period	1,532	2,190	5,421	5,131

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Interim Condensed Consolidated and Bank Financial Statements
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BALANCE SHEET

(all amounts in thousands of Lats)

	30/09/08		31/12/07	
	Group	Bank	Group	Bank
<u>Assets</u>				
Cash and balances with Central Bank	46,710	46,710	66,265	66,265
Trading securities	4,366	4,366	3,269	3,269
Investment securities – held to maturity	14,981	14,981	13,060	13,060
Investment securities – available for sale	64,295	64,124	54,131	54,131
Due from credit institutions	89,401	89,006	104,871	104,662
Derivative financial instruments	142	142	84	84
Loans to customers	730,946	715,243	667,858	660,350
Investment properties	2,116	2,116	2,116	2,116
Investments in subsidiaries and associated undertakings	332	900	552	922
Intangible fixed assets	2,421	1,927	2,018	1,927
Property and equipment	8,821	7,836	8,975	7,947
Other assets	4,194	826	3,580	1,005
Deferred expenses and accrued income	804	606	811	689
Total assets	969,529	948,783	927,590	916,427
<u>Liabilities</u>				
Due to credit institutions	542,006	522,985	497,302	488,738
Due to customers	277,336	277,834	282,124	282,550
Derivative financial instruments	810	810	130	130
Transit funds	2,467	2,467	2,575	2,575
Issued debt securities	40,269	40,269	52,494	52,494
Other liabilities	10,803	10,167	11,963	11,211
Deferred income and accrued expenses	2,650	1,949	2,789	2,082
Current income tax liabilities	-	-	49	-
Deferred tax liabilities	963	936	963	936
Subordinated liabilities	31,544	31,544	13,302	13,302
Total liabilities	908,848	888,961	863,691	854,018
<u>Shareholder's equity</u>				
Share capital	48,513	48,513	48,513	48,513
Reserve capital	2,524	2,063	2,524	2,063
Minority interest	27	-	-	-
Revaluation deficit on available for sale investments	(4,658)	(4,658)	(1,540)	(1,540)
Retained earnings	14,275	13,904	14,402	13,373
Total shareholder's equity	60,681	59,822	63,899	62,409
Total liabilities and shareholder's equity	969,529	948,783	927,590	916,427
<u>Off balance sheet items</u>				
Contingent liabilities	22,176	22,176	11,456	11,456
Financial commitments	43,740	70,514	42,495	66,125

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CONSOLIDATED STATEMENT OF CHANGES IN THE GROUP'S EQUITY

(all amounts in thousands of Lats)

	Share Capital	Reserve capital	Minority interest	Revaluation deficit on available for sale investments	Retained earnings	Total equity
Balance as at 31 December 2007	48,513	2,524	-	(1,540)	14,402	63,899
Distribution of profit – payment for use of state capital	-	-	-	-	(1,659)	(1,659)
Net loss on available for sale investments	-	-	-	(3,118)	-	(3,118)
IPS „Hipo fondi” other minority shareholders	-	-	27	-	-	27
Profit for the period	-	-	-	-	1,532	1,532
Balance as at 30 September 2008	48,513	2,524	27	(4,658)	14,275	60,681

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

(all amounts in thousands of Lats)

	Share Capital	Reserve capital	Revaluation deficit on available for sale investments	Retained earnings	Total equity
Balance as at 31 December 2007	48,513	2,063	(1,540)	13,373	62,409
Distribution of profit – payment for use of state capital	-	-	-	(1,659)	(1,659)
Net loss on available for sale investments	-	-	(3,118)	-	(3,118)
Profit for the period	-	-	-	2,190	2,190
Balance as at 30 September 2008	48,513	2,063	(4,658)	13,904	59,822

Mortgage and Land Bank of Latvia
Interim Condensed Consolidated and Bank Financial Statements
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CASH FLOW STATEMENT

(all amounts in thousands of Lats)

	9 months to 30 September 2008		9 months to 30 September 2007	
	Group	Bank	Group	Bank
Cash flows from operating activities				
Profit before taxation	2,148	2,757	6,619	6,190
Depreciation and amortisation	1,772	1,525	1,799	1,698
Increase / (decrease) in provision for impairment losses	3,190	2,755	736	491
(Profit) / loss from foreign exchange revaluation	(49)	(20)	-	30
(Profit) / loss from sale of property and equipment	(136)	(1)	(1)	(1)
Increase in deferred income and accrued expenses	(104)	(81)	1,076	934
(Increase) / decrease in deferred expenses and accrued income	7	83	(104)	(107)
(Increase) in other assets	(3,773)	(2,980)	(1,253)	(1,449)
Increase in other liabilities	(480)	(364)	6,504	6,302
Increase in cash and cash equivalents from operating activities before changes in assets and liabilities	2,575	3,674	15,376	14,088
Increase in balances due from credit institutions	(13,020)	(13,020)	(14,695)	(14,695)
Increase in loans to customers	(64,875)	(56,246)	(129,623)	(131,715)
Increase in trading securities	(1,097)	(1,097)	1,562	1,562
Increase in balances due to credit institutions	15,775	5,188	125,381	127,588
Increase in balances due to customers	(4,788)	(4,716)	8,814	9,285
Decrease in transit funds	(108)	(108)	(110)	(110)
Increase in debt securities issued	(12,225)	(12,225)	8,719	8,719
Increase in cash and cash equivalents from operating activities	(77,763)	(78,550)	15,424	14,722
Corporate income tax	(674)	(619)	(1,747)	(1,400)
Cash flows from investing activities				
Increase in investment securities	(13,504)	(13,333)	(2,596)	(2,596)
Purchases of property and equipment	(2,003)	(1,427)	(3,374)	(2,537)
Proceeds from property and equipment disposal	118	14	22	7
Acquisition of investments in associated entities	220	22	-	(500)
Cash and cash equivalents used in investing activities	(15,169)	(14,724)	(5,948)	(5,626)
Cash flows from financing activities				
Proceeds from subordinated debt	18,242	18,242	-	-
Dividend paid	(1,659)	(1,659)	(1,400)	(1,400)
Cash and cash equivalents used in financing activities	16,583	16,583	(1,400)	(1,400)
Increase in cash and cash equivalents	(77,023)	(77,310)	6,329	6,296
Cash and cash equivalents at the beginning of the period	131,936	131,857	121,395	121,322
Effect of exchange rates on cash and cash equivalents	49	20	-	(30)
Cash and cash equivalents at the end of the period	54,962	54,567	127,724	127,588

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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.

RISK MANAGEMENT

The Group and the Bank manages all the major risks affecting the operation of the Group and the Bank in accordance with the Risk Management Policy approved by the Council of the Bank. The Risk Management Policy stipulates and describes the aggregate of measures used to ensure that a possibility of suffering losses is minimised in the event the invested or receivable resources would not be repaid or recovered in due time or full amount or the Group or the Bank would suffer other losses or would not derive the planned profit.

The Group and the Bank abides by the following principles in its risk management:

- while assuming the risks the Group and the Bank shall be capable of implementing the aims and assignments defined in its development strategy in a longer run;
- the Group and the Bank shall operate by maintaining an optimum balance between profitability and safeguarding against the risks, i.e. the profitability must be as large as possible, however, the Group and the Bank shall not be exposed to the risks;
- risk assessment and management shall be an integral component of the every-day functions of the Group and the Bank;
- in accordance with their authority and competence the employees of the Group and the Bank shall know a customer and understand fully the nature of each transaction (operation) to be able to identify and assess the risks associated with the transaction (operation) and find the best solution both for the customer and the Group or the Bank;
- the Group and the Bank shall assess the probable losses that it might incur by assuming the risks and avoid extraordinary losses in its operation;
- the Group and the Bank shall identify and assess the probable risks before launching of new products or services or entering new markets;
- where necessary, the Group and the Bank shall reduce the risk limits, sell the assets subject to the risk or even leave the respective markets should these be assessed as excessively risky.

In managing the risks the Group and the Bank applies various methods for measuring the risks, sets the limits and maintains the appropriate controls. All risk policies are approved by the Council.

Credit Risk

The Group and the Bank is subject to the credit risk. The credit risk is the risk of the customer or co-operation partner not being able to or refusing to meet its liabilities towards the Group or the Bank in full amount and due time.

The Group and the Bank manages the credit risk according to the Credit Policy as well as internal regulations, procedures and instructions of credit operations.

RISK MANAGEMENT (continued)

The Credit Policy of the Bank describes and defines the principles for the management of the credit risk and it relates to all activities of the Group and the Bank involving credit risk – lending, financial market transactions (operations), intermediary activities on behalf of the clients and issue of guarantees to third parties.

The Bank's Risk Management Committee monitors the credit risk, including credit risk concentrations, and the quality of the credit portfolio, whereas central, regional and branch credit committees are taking decisions on the credit risk within the approved limits. The Bank's Risk Management Department is responsible for analysis of the credit risk concentration, setting and controlling the limits as well as the evaluation of the quality of the credit portfolio, whereas the Bank's Loan Department and Treasury Department is responsible for daily credit risk management in lending operations and operations with financial instruments respectively.

The Group and the Bank monitors the credit risk by assessing the creditworthiness and adequacy of collateral of the customer or counterparty on a regular basis as well as controls the credit risk at the level of customer, related customers and sectors of economy according to the risk limits set at the Group and the Bank.

The Group and the Bank manages credit risk concentrations according to the Risk Exposures Controlling Policy that stipulates the methods of analysis of the credit risk concentrations and its controlling instruments including limits on credit risk concentrations. Credit risk concentrations is managed by measuring and setting limits on the following concentrations:

- ratio of large exposure concentration and own funds (internal limit - 400%, limit set by the Law on Credit Institutions – 800%), as of 30.09.2008. was 47% (as of 31.12.2007.-79%);
- ratio of single client's (related clients' group) large exposure and own funds, which can not exceed 25%, as of 30.09.2008. was 14.4% (as of 31.12.2007.-16.6%);
- proportion of risk concentration in single economic sector in the Bank's credit portfolio and own funds as of 30.09.2008. was 185.5% (as of 31.12.2007.-195.9%);
- ratio of risk exposures with persons related to the Bank and own funds, which can not exceed 15%, as of 30.09.2008. was 2.3% (as of 31.12.2007.-6.1%).

Since the Bank's strategy is not focused on servicing the non-residents business, the proportion of the Bank's total claims to non-residents was small and as of 30.09.2008. was 7.4% (as 31.12.2007.-7.7%) of the Bank's total assets. The Group and the Bank manages the country risk that results from the lending operations to non-residents according to the Country Risk Management Policy.

Liquidity Risk

The liquidity risk relates to the ability of the Group and the Bank to redeem the legally valid claims of its customers and other creditors in due time and secure that the increase of the anticipated claims presents reasonable costs. The Liquidity Risk Management Policy of the Bank stipulates the principles for management of liquidity risk. The Bank shall ensure that the liquid assets are not less than 30% (set by the FCMC) of its short-term liabilities at all times. The Assets and Liabilities Committee of the Bank stipulates the guidelines for liquidity risk management and controls compliance thereof, whereas the Treasury Department provides for daily management of the liquidity risk. To evaluate the liquidity risk, the Bank uses the GAP method. The Bank has set liquidity net position limit in each significant currency and total liquidity net position limit as well as maximum deposit amount from a single depositor to control the liquidity risk. Liquidity ratio (min – 30%) as of 30.09.2008. was 78.8% (as of 31.12.2007.-101.7%).

Foreign Currency Risk

The foreign currency risk occurs due to the differences between the asset and liability positions of foreign currencies that, as a result of the fluctuations of the exchange rates, affect the cash flow and financial results of the Group and the Bank. The Currency Risk Management Policy of the Bank stipulates the principles for the management of the foreign currency risk.

The Group and the Bank controls the foreign currency risk by imposing limits on the open currency positions for each currency and all currencies together consolidating in lats and by complying with the open currency position limits established in the law On Credit Institutions.

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RISK MANAGEMENT (continued)

The Assets and Liabilities Committee of the Bank stipulates the guidelines for foreign currency risk management and controls compliance thereof, whereas the Treasury Department provides for daily management of the foreign currency risk.

Interest Rate Risk

The interest rate risk is related to the influence of the fluctuations of the market rates onto the interest income and expenses of the Group and the Bank. To assess the interest rate risk the Bank analyses the maturity structure of the assets and liabilities sensitive to the changes in interest rates and susceptibility of the maturity structure to the potential fluctuations of the interest rates on a regular basis.

The Assets and Liabilities Management Committee monitors the interest rate risk, whereas the Treasury Department is responsible for the daily management of the interest rate risk. The Bank has set limit on changes in economic value of the Bank at 10% of own funds and limit on changes in net interest income at 2% of own funds which as of 30.09.2008. were 9.8% (as of 31.12.2007.-7.96%) and 1.54% (as of 31.12.2007.-0.93%) respectively.

Operational risk

The operational risk results from intentional or unintentional deviations from the standards adopted in daily operation of the Group and the Bank, for example human mistake or fraud, disturbances in the operation of the information systems, insufficient control procedures or their ignorance. The Group and the Bank manages operational risk according to the Operational Risk Management Policy. The Internal Control System provides for management and control of the operational risk in the Group and the Bank. The Group and the Bank uses self-assessment method to measure the operational risk, whereas the Bank's operational risk information system is used to identify, analyse and control the operational risk. The structural units of the Group and the Bank are responsible for the management of the operational risk in the daily operations, but the Risk Management Committee monitor the operational risk. The Risk Management Department is responsible for the implementation of operational risk management in the Group and the Bank.

The Bank has implemented Business continuity plan that includes guidelines on actions to be taken by the Bank, its structural units and employees at occurrence of risks that can have substantial negative effect on the Bank's operations.

Capital Adequacy

Capital adequacy shows those capital resources of the Group and the Bank needed to cover the credit and market risks arising from asset-side and off-balance sheet positions.

As at 30 September 2008 the capital adequacy ratio of the Bank calculated according to the regulations of the Financial and Capital Market Commission were 9.2% (as of 31.12.2007.-9.9%) which exceeded the minimum of 8%.

1. Capital requirements	30/09/2008	31/12/2007
Credit risk capital requirement	65,467	56,746
Market risk capital requirement	-	-
Operational risk capital requirement	3,539	-
2. Capital adequacy		
Total capital requirements (CR+MR+OR)	69,006	56,743
Own funds	79,441	70,482
Surplus of own funds	10,435	13,739
Capital adequacy	9.2%	9.9%

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THE PERFORMANCE RATIOS OF THE BANK

Items	Accounting period	Previous accounting year
Return on equity (ROE) (%)	4.66%	10.58%
Return on assets (ROA) (%)	0.31%	0.78%

CONSOLIDATION GROUP

No	Name of commercial company	Code of place of registration, address of registration	Type of activity of commercial company *	Share of fixed capital (%)	Voting rights in commercial company (%)	Justification for including in the Group**
1.	SIA „Hipotēku bankas nekustamā īpašuma aģentūra”	LV –Latvija 40003426895	CKS	100	100	MS
2.	SIA „Rapsis”	LV – Latvija 50003614071	CKS	100	100	MS
3.	SIA „Hipolīzings”	LV – Latvija 40003616329	CFI	100	100	MS
4.	SIA „Risku investīciju sabiedrība”	LV – Latvija 40003952445	CFI	100	100	MS
5.	IPS „Hipo fondi”	LV – Latvija 40003403040	IPS	83	83	MS
6.	SIA „Rīgas Centra namu pārvalde”	LV – Latvija 40003266805	CKS	100	100	MS
7.	KS "Mazo un vidējo komersantu atbalsta fonds"	LV – Latvija 40003681329	CFI	47.62	47.62	KS

* IPS – investment management company, CFI – other financial institution, CKS – other commercial company.

** MS – subsidiary; KS – joint venture.

RATINGS ASSIGNED TO BANK BY RATING AGENCY MOODY'S INVESTORS SERVICE

Rating type	Ratings	Rating Approval date	Previous rating
For long-term foreign currency bank deposits	A2	10.07.2008.	A2
For short-term foreign currency deposits	P1	10.07.2008.	P1
The financial strength rating	D-	10.07.2008.	D-
The rating of mortgage bonds issued	A1	10.07.2008.	A1

Moody's Investors Service reports of the Bank may be found at: www.hipo.lv

Additional information on the ratings assigned (incl. Legend of ratings) may be found at: www.moodys.com

These interim financial reports are to be viewed along with the Bank's Annual Report for 2007.

Inesis Feiferis
Chairman of the Board

Uvis Zemītis
Chief Accountant