

**MORTGAGE AND LAND BANK
OF LATVIA**

**Interim Condensed Consolidated and Bank Financial
Statements for the three months period ended 31 March 2010
(unaudited)**

MORTGAGE AND LAND BANK OF LATVIA MANAGEMENT REPORT

3 months of 2010

Having experienced a rapid decline in 2009 the economy of Latvia stabilised in the 1st quarter of 2010. Nevertheless, unemployment keeps rising and attained 17.3% at the end of March (16.0% at the beginning of year). In the first months of 2010 the external trade balance of Latvia has retained a positive balance. The government of Latvia complies with the requirements of the international lenders achieving considerable fiscal consolidation. As a result, the international rating agencies upgraded the outlooks of the credit ratings of Latvia in the 1st quarter of 2010.

In the 1st quarter of 2010 the assets of the commercial banks of Latvia decreased by 1%, totalling to 21.5 bln lats at the end of March, the loan portfolio – by 1.7%, deposits (with transit funds) – by 2.5%, but capital and reserves – by 2%. In the given period the losses of the banks amounted to 133.4 mln lats mostly caused by accumulation of provisions for loans not yielding profit.

The gross assets of the Mortgage Bank increased by 8.8 mln lats or 1% in the 1st quarter of 2010 amounting to 975.4 mln lats. Within the first three months of 2010 the gross loan portfolio of the Mortgage Bank has diminished by 3%, reaching 685.5 mln lats comprised of the development loans' portfolio in the amount of 274 mln lats (40 % of the portfolio) and commercial loans' portfolio in the amount of 411.5 mln lats (60% of the portfolio). The deposits have not changed significantly during the period (320 mln lats). In the 1st quarter the Bank made provisions for insecure assets in the amount of 11 mln lats resulting in 9.73 mln lats of unaudited losses. As at 31 March 2010 the ratio of the Bank's provisions and loan portfolio was 11.4%.

Various changes to the composition of council and board of the Mortgage Bank took place in the 1st quarter of 2010. On the 1st of March 2010 a new council of the Mortgage Bank was elected for a period of three years consisting of: Baiba Bāne, Dāvids Tauriņš and Jānis Pone. On the 23rd of March Dāvids Tauriņš resigned from his post in the council. On the 8th of April Mārtiņš Bičevskis – the state secretary of the Ministry of Finance acting as the representative of the shareholder of the Mortgage Bank – Ministry of Finance appointed Andžs Ūbelis to the post of Dāvids Tauriņš. Thus, the council of the Mortgage Bank consists of: Baiba Bāne – chairperson of the council, Andžs Ūbelis – deputy chairperson and Jānis Pone – member of the council.

On the 12th of March the council appointed Baiba Brigmane and Gints Āboltiņš to the board of the Mortgage Bank. The board of the Mortgage Bank consists of: Rolands Paņko – chairman of the board, Jēkabs Krieviņš – deputy chairman of the board and board members - Baiba Brigmane, Jānis Bērziņš and Gints Āboltiņš.

In the 1st quarter of 2010 the Mortgage Bank, as commissioned by the government, proceeded with implementation of the following aid programmes providing support to specific groups of entrepreneurs and population:

- Programme for improvement of competitiveness of businesses;
- Micro lending programme;
- Start programme „Support to self-employment and business start-ups”.

Programme for improvement of competitiveness of businesses

In 2009 to finance the programme the Mortgage Bank obtained a 100 mln euro (70 mln lats) loan from the Nordic Investment Bank (NIB). There was also a Loan Fund established consisting of the public financing – 61.6 mln euro (43.3 mln lats) and financing of the Mortgage Bank – 21.6 mln euro (15.2 mln lats). By the end of March 2010 the Programme for improvement of competitiveness of businesses had granted loans for 114.4 mln lats, including 33.75 mln lats from the resources of the Loan Fund.

Micro lending programme

The total financing volume of the programme is 564.8 thsd lats. By the end of March, 2010 the Mortgage Bank had granted microloans for the total amount of 479 thsd lats.

Programme „Support to self-employment and business start-ups”

By the end of March 2010, 676 applicants had applied for consultations and training, 162 participants of the programme had completed their training, 185 business plans were submitted to the bank of which 136 were examined by the credit committee and financial support was granted to 57 projects for the total loan amount of 1.17 mln lats.

In February 2010 the Bank launched SME development lending programme for micro, small and medium enterprises and agricultural co-operative unions. The purpose of the programme is to enhance access to the financing for the enterprises registered in Latvia to revive and promote development of the national economy of Latvia. On the 2nd of October 2009 to implement the programme the Mortgage Bank concluded a 100 mln euro loan agreement with the European Investment Bank. In February 2010 the Mortgage Bank received the first tranche of the loan in the amount of 50 mln euro. By the end of March the SME development programme had granted loans for 0.55 mln lats.

**MORTGAGE AND LAND BANK OF LATVIA
MANAGEMENT REPORT**

(continued)

The beginning of 2010 is marked with a positive assessment of the economic development potential of Latvia acknowledged also by international rating agencies *Standard & Poor's Rating Services* and *Moody's Investors Service Ltd* through upgrading from negative to stable of the credit rating outlook of Latvia. The Mortgage Bank is 100% state-owned bank and its rating is directly linked to sovereign rating of Latvia. Having upgraded the rating outlook for Baa3 assigned to Latvia's local and foreign currency ratings, the *Moody's Investors Service Ltd* also notched up from negative to stable the outlook of Mortgage Bank's long-term foreign currency deposits rating Baa3. The Mortgage Bank is assigned the following ratings:

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

which are investment grade ratings.

Throughout the 1st quarter of 2010 the Mortgage Bank serviced its customers in 27 branch offices and 8 sub-branches located in Riga and other cities of Latvia.

**MORTGAGE AND LAND BANK OF LATVIA
THE SUPERVISORY COUNCIL AND BOARD OF DIRECTORS OF THE BANK**

Supervisory Council (at 31 March 2010)

Baiba Bāne	Chairman of the Council
Jānis Pone	Member of the Council

During the reporting period Ms. Baiba Brigmane and Mr. Dāvids Tauriņš resigned from the Council and Mr. Jānis Pone was appointed as member of the Council.

Supervisory Council (from 8 April 2010)

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

After the reporting period Mr. Andžs Ūbelis was appointed as member of the Council.

Board of Directors (at 31 March 2010)

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

During the reporting period Andris Riekstiņš resigned from the Board and Baiba Brigmane and Gints Āboltiņš as were appointed as members of the Board.

STATEMENT OF RESPONSIBILITY OF THE MANAGEMENT

Management is responsible for preparing financial statements from the books of prime entry of the Group and the Bank for each financial period that present fairly the state of affairs of the Group and the Bank as at the end of the financial period and the results of their operations and cash flows for that period according to the International Financial Reporting Standards as adopted by the European Union..

Management confirms that suitable accounting policies have been used and applied consistently and reasonable and prudent judgments and estimates have been made in the preparation of the interim condensed consolidated and bank financial statements for the period ended 31 March 2010. Management also confirms that applicable International Financial Reporting Standards as adopted in EU have been used in preparation of the financial statements and that these financial statements have been prepared on a going concern basis. Appropriate accounting policies have been applied on a consistent basis.

Management is responsible for keeping proper accounting records, for taking reasonable steps to safeguard the assets of the Group and the Bank and to prevent and detect fraud and other irregularities. Management is also responsible for managing the Bank in compliance with the Law on Credit Institutions, regulations of the Bank of Latvia and the Financial and Capital Market Commission as well as other legislation of the Republic of Latvia.

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INCOME STATEMENT
(all amounts in thousands of Euro)

	3 months to 31 March 2010		3 months to 31 March 2009	
	Group	Bank	Group	Bank
Interest income	15,007	14,547	21,830	21,014
Interest expense	(11,609)	(11,619)	(13,576)	(13,181)
Net interest income	3,398	2,928	8,254	7,833
Fee and commission income	1,579	1,392	1,457	1,342
Fee and commission expense	(297)	(285)	(336)	(285)
Net fee and commission income	1,282	1,107	1,121	1,057
Dividend income	-	-	-	-
Net trading income	593	611	2,280	2,211
Other operating income	3,564	2,954	1,583	1,397
Staff costs	(3,256)	(2,907)	(3,660)	(3,277)
Administrative expenses	(2,594)	(2,151)	(2,839)	(2,410)
Depreciation and amortisation	(696)	(636)	(756)	(676)
Provision for impairment losses	(15,588)	(15,753)	(5,351)	(5,146)
Profit before income tax	(13,297)	(13,847)	632	989
Income tax expense	-	-	(300)	(262)
Net profit for the period	(13,297)	(13,847)	332	727
Attributable to:				
Equity holders of the Bank	(13,304)	-	-	-
Minority interest	7	-	-	-

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BALANCE SHEET

(all amounts in thousands of Euro)

	31/03/10		31/12/09	
	Group	Bank	Group	Bank
<u>Assets</u>				
Cash and balances with Central Bank	89,988	89,988	136,591	136,591
Trading securities	1,853	1,602	7,220	6,999
Investment securities – held to maturity	57,521	57,521	61,161	61,161
Investment securities – available for sale	141,236	141,236	70,990	70,990
Due from credit institutions	78,087	77,844	50,385	50,193
Derivative financial instruments	1,128	1,128	2,780	2,780
Loans to customers	856,316	868,979	900,224	909,928
Investment properties	1,659	1,659	1,659	1,659
Investments in subsidiaries and associated undertakings	398	2,174	398	2,174
Intangible assets	3,001	2,316	3,136	2,449
Property and equipment	10,297	9,432	10,723	9,812
Current income tax assets	-	-	-	-
Other assets	17,028	3,628	12,658	2,654
Deferred expenses and accrued income	802	561	942	757
Total assets	<u>1,259,314</u>	<u>1,258,068</u>	<u>1,258,867</u>	<u>1,258,147</u>
<u>Liabilities</u>				
Due to credit institutions	464,559	464,559	539,997	539,997
Due to customers	450,033	450,525	462,076	462,164
Derivative financial instruments	13	13	221	221
Transit funds	2,789	2,789	2,775	2,775
Issued debt securities	50,303	50,871	53,257	54,423
Other liabilities	139,717	139,204	38,986	38,182
Deferred income and accrued expenses	5,497	4,509	5,687	4,804
Current income tax liabilities	18	-	61	-
Deferred tax liabilities	48	-	38	-
Subordinated liabilities	44,869	44,869	44,236	44,236
Total liabilities	<u>1,157,846</u>	<u>1,157,339</u>	<u>1,147,334</u>	<u>1,146,802</u>
<u>Shareholder's equity</u>				
Share capital	172,624	172,624	172,624	172,624
Reserve capital	3,591	2,935	3,591	2,935
Minority interest	64	-	57	-
Revaluation deficit on available for sale investments	(1,085)	(1,085)	(4,317)	(4,317)
Retained earnings	(73,726)	(73,745)	(60,422)	(59,897)
Total shareholder's equity	<u>101,468</u>	<u>100,729</u>	<u>111,533</u>	<u>111,345</u>
Total liabilities and shareholder's equity	<u>1,259,314</u>	<u>1,258,068</u>	<u>1,258,867</u>	<u>1,258,147</u>
<u>Off balance sheet items</u>				
Contingent liabilities	23,660	26,667	17,188	20,196
Financial commitments	26,696	65,522	46,865	78,726

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CONSOLIDATED STATEMENT OF CHANGES IN THE GROUP'S EQUITY

(all amounts in thousands of Euro)

	Attributable to equity holders				Minority interest	Total equity
	Share Capital	Reserve capital	Revaluation deficit on available for sale investments	Retained earnings		
Balance as at 31 December 2009	172,624	3,591	(4,317)	(60,422)	57	111,533
Net profit on available for sale investments	-	-	3,232	-	-	3,232
Loss for the period	-	-	-	(13,304)	7	(13,297)
Balance as at 31 March 2010	172,624	3,591	(1,085)	(73,726)	64	101,468

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

(all amounts in thousands of Euro)

	Share Capital	Reserve capital	Revaluation deficit on available for sale investments	Retained earnings	Total equity
	Balance as at 31 December 2009	172,624	2,935	(4,317)	(59,897)
Net profit on available for sale investments	-	-	3,232	-	3,232
Loss for the period	-	-	-	(13,848)	(13,848)
Balance as at 31 March 2010	172,624	2,935	(1,085)	(73,745)	100,729

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CASH FLOW STATEMENT

(all amounts in thousands of Euro)

	3 months to 31 March 2010		3 months to 31 March 2009	
	Group	Bank	Group	Bank
Cash flows from operating activities				
(Loss) / profit before taxation	(13,297)	(78,339)	632	989
Depreciation and amortisation	696	2,610	756	676
Increase in provision for impairment losses	10,747	94,176	3,738	3,622
(Profit) / loss from sale of property and equipment	(6)	115	(100)	13
Increase in deferred income and accrued expenses	381	2,126	627	636
Decrease in deferred expenses and accrued income	139	46	(390)	(350)
(Increase) / decrease in other assets	662	1,725	1,191	1,922
Increase in other liabilities	100,524	20,013	406	498
Increase in cash and cash equivalents from operating activities before changes in assets and liabilities	99,846	42,472	6,860	8,006
Decrease / (increase) in balances due from credit institutions	3,177	43,075	5,710	5,710
Decrease / (increase) in loans to customers	32,921	32,877	21,973	22,432
Decrease in trading securities	5,367	(1,743)	2,325	2,349
(Decrease) / increase in balances due to credit institutions	(87,531)	(173,726)	(48,607)	(48,847)
Increase in balances due to customers	(12,043)	32,160	8,200	8,125
Decrease in transit funds	-	(464)	43	43
Decrease in debt securities issued	(2,954)	(3,431)	(415)	(415)
Cash and cash equivalents used in operating activities	38,783	(28,780)	(3,911)	(2,597)
Corporate income tax paid	43	-	-	-
Cash flows from investing activities				
Increase in investment securities	(66,514)	(6,232)	11,302	11,308
Purchases of property and equipment	(138)	(1,386)	(542)	(461)
Proceeds from property and equipment disposal	9	31	394	3
Proceeds from disposal of investments in associated entities	-	-	71	-
Acquisition of investments in associated entities	-	(1,231)	-	(1,231)
Cash and cash equivalents used in investing activities	(66,643)	(8,818)	11,225	9,619
Cash flows from financing activities				
Shareholders cash contribution	-	103,596	42,000	42,000
Proceeds from subordinated liabilities	-	-	-	-
Subordinated liabilities repaid	-	-	-	-
Dividend paid	-	(1,374)	(859)	(859)
Cash and cash equivalents generated from financing activities	-	102,222	41,141	41,141
Increase / (decrease) in cash and cash equivalents	(27,817)	64,624	48,455	48,163
Cash and cash equivalents at the beginning of the year	144,171	81,856	81,753	81,856
Cash and cash equivalents at the end of the year	116,354	146,480	130,208	130,019

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 minimized 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. Risk management is an integral component of the internal control system of the Group and the Bank and the risk management system has been established taking into account the size and structure of the Group and the Bank, as well as the best advisable practice, incl. the guidelines of Basel bank supervisory committee.

In light of the changes occurring on global financial markets and economy, a number of major improvements were made to the risk management system of the Group and the Bank during the reporting period, thus allowing to identify the risks more precisely and timely and to determine their impact on the future operations of the Group and the Bank.

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 apply various methods and instruments for measuring risks, set the limits and maintain 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.

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.

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RISK MANAGEMENT (continued)

Management process of credit risk within the Group and the Bank encompasses establishment of guidelines and limitations, granting of loans or setting limits to particular clients or groups of interrelated clients; administration, monitoring and evaluation of files of clients or interrelated client groups, as well as appropriate control of the process, operation of management information system and evaluation of the total efficiency of the process.

In establishment of guidelines and limitations, the Group and the Bank primarily follows the common strategy of the Group and the Bank, as well as their historic experience in credit risk management, which allows defining adequate limitations of concentration, as well as adequate assessment of creditworthiness and collateral, passing decisions in decision-making institutions of the appropriate level. As the common strategy of the Group and the Bank encompasses gradual transformation of the Bank into development bank, the risk stemming from implementation of framework funding programmes becomes an increasingly significant risk source for the Group and the Bank.

The Bank's Lending department bears the responsibility for daily credit risk management in lending operations, incl. when setting criteria of creditworthiness and collateral adequacy, while decisions about assuming credit risk within the set limits are made by branch, regional and the Central lending committees, or the Board of the Bank. The daily supervision and administration of loans is conducted on the basis of each individual borrower's risk grade and affiliation, determined by organizational structure of the Group and the Bank.

The Risk management committee conducts the integrated monitoring of credit risk, incl. credit risk concentration and loan portfolio quality, while the Risk management department bears the responsibility for analysis of credit risk concentration, setting of limits and their control, quality assessment of the loan portfolio and building of provisions, as well as daily management of credit risk in operations with financial instruments. At least once a year, stress testing of the loan portfolio and scenario analysis is conducted, that includes changes of various macro-environment affecting factors (drop of real estate property prices, households' income decrease, contingent changes in development of various industries of national economy, and similar) and demonstrates the eventual impact on the Group's and the Bank's profitability, loan portfolio quality, volume of provisions and level of capital adequacy.

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 concentration 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 31.03.2010 was 55.9% (as of 31.12.2009 – 47.1%);
- ratio of single client's (related clients' group) large exposure and own funds, which may not exceed 25%, as of 31.03.2010 was 24.3% (as of 31.12.2009 – 20.7%);
- ratio of risk exposures with persons related to the Bank and own funds, which may not exceed 15%, as of 31.03.2010 was 2.5% (as of 31.12.2009 – 2.6%);
- proportion of risk concentration in a single economic sector in the Bank's credit portfolio and own funds as of 31.03.2010 was 116.6% (as of 31.12.2009 – 120.9%);

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 31.03.2010 was 9.8% (as 31.12.2009 – 7.1 %) 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.

Each of the structural units involved in credit risk management maintain an appropriate internal control, efficiency of which is responsibility of the Internal audit department.

The management of the Group and the Bank has performed calculation of losses on the basis of all the facts at its disposal, unbiased proofs of depreciation, and believes the calculations disclosed in the financial reports are reasonable, considering the available information. Nonetheless, having the present awareness, it might occur, as a result of the next year's actual events, differing from the assumptions, that the respective book values of assets and liabilities be corrected.

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 principles for management of liquidity risk are determined by the Liquidity Risk Management Policy and Business Continuity Plan for Liquidity Crisis Situation. The Bank maintains that the liquid assets do not fall below 30% (set by the FCMC) of its short-term liabilities at all times.

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RISK MANAGEMENT (continued)

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. At least once a month, scenario analysis or stress testing is conducted, to reveal the impact of contingencies on liquidity of the Group and the Bank.

Compliance with the liquidity ratio (min – 30%) was 88.7% as of 31.03.2010 (as of 31.12.2009 – 82.2%).

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 principles for the management of the foreign currency risk are outlined in the Currency Risk Management Policy of the Bank.

Monitoring of the foreign currency risk is conducted by the Assets and Liabilities Management Committee of the Bank, whereas the Treasury Department provides for daily management of the foreign currency risk.

The Group and the Bank maintains a cautious foreign currency risk management policy and 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.

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 Group and 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, respectively, were 8.6% as of 31.03.2010 (as of 31.12.2009 – 7.6%) and 0.2% (as of 31.12.2009 – 0.4%).

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. Self-assessment method is used to measure the operational risk, whereas the Bank's operational risk information system is used to identify, analyse and control the operational risk, which registers and analyses occurrences of operational risk and calculates the scale of actual or potential losses. 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 supervises the operational risk. The Risk Management Department is responsible for implementation of the 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 and also against operational risks.

The Group and the Bank completely follows the requirements of Basel II in their capital adequacy evaluation process. The Group and the Bank uses the standardised approach to calculate minimum capital charge for credit and market risks and basic indicator approach – for operational risk.

As of 31.03.2010, the capital adequacy ratio of the Bank calculated according to the regulations of the Financial and Capital Market Commission were 12.2% (as of 31.12.2009 - 12.8%) which exceeded the minimum of 8% for the ratio of the own capital and total of risk-weighted assets and off-balance sheet items.

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RISK MANAGEMENT (continued)

The Group and the Bank also conducts the internal capital adequacy evaluation process (ICAAP), calculating capital requirements for those significant risks which do not have minimum regulatory capital requirements determined. The results of the internal capital adequacy evaluation as of 31.03.2010 were as follows:

	31/03/10 Bank
Capital base for internal capital adequacy evaluation	89,500
Total internal capital requirement	82,451
Internal capital adequacy ratio	8.7%
Surplus of capital base	7,049

THE PERFORMANCE RATIOS OF THE BANK

Items	Accounting period	Previous accounting year
Return on equity (ROE) (%)	-50.66%	-65.02%
Return on assets (ROA) (%)	-4.01%	-5.60%

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 „Hipolīzings”	LV – Latvija 40003616329	CFI	100	100	MS
3.	SIA „Risku investīciju sabiedrība”	LV – Latvija 40003952445	CFI	100	100	MS
4.	IPS „Hipo fondi”	LV – Latvija 40003403040	IPS	83	83	MS
5.	SIA „Rīgas Centra namu pārvalde”	LV – Latvija 40003266805	CKS	100	100	MS
6.	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	Baa3	25.06.2009.	Baa3
For short-term foreign currency deposits	P3	25.06.2009.	P3
The financial strength rating	E+	25.06.2009.	D-
The rating of mortgage bonds issued	Baa2	23.04.2009.	A2

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.moody.com

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POST BALANCE SHEET EVENTS

In accordance with the decision of the bank's shareholder, the Bank has increased its fixed capital by LVL 70,28 mln. Thus the total volume of the fixed capital has reached LVL 191,60 mlj. The increase of fixed capital was performed according the state budget law for year 2010.

These condensed financial reports are to be viewed along with the Bank's Annual Report for 2009.

Rolands Paņko
Chairman of the Board

Uvis Zemītis
Chief Accountant