

AS Meridian Trade Bank

Annual report

for the year ended 31 December 2018

CONTENTS

	page
MANAGEMENT REPORT	3-5
INFORMATION ON THE BANK'S MANAGEMENT	6
STATEMENT OF RESPONSIBILITY OF THE BANK'S MANAGEMENT	7
BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS:	
BANK'S SEPARATE AND GROUP'S CONSOLIDATED STATEMENT OF FINANCIAL POSITION	8
BANK'S SEPARATE AND GROUP'S CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME	9
BANK'S SEPARATE AND GROUP'S CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY	10
BANK'S SEPARATE AND GROUP'S CONSOLIDATED STATEMENT OF CASH FLOWS	11
NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS	12-82
INDEPENDENT AUDITORS' REPORT	83-90

MANAGEMENT REPORT

Dear customers, partners and shareholders,

The Board and the Council of the AS Meridian Trade Bank (hereinafter – the Bank) is reporting on the results for 2018.

During the reporting period, the Bank continued the reorganisation of its business activities, implementing the goals set in its development strategy in accordance with the current situation in the national economy and financial market.

General situation in the Latvian banking sector

2018 was complex and challenging year for the Latvian banking sector as a whole and for the Bank in particular. The biggest turmoil in Latvia's financial sector was caused by the announcement by the US Treasury Financial Crime Prevention Network (FinCEN) regarding possible violations by one of the largest Latvian banks, which, after some time, resulted in self-liquidation of the bank. The industry underwent fast and radical changes - the regulator launched a review of international customer servicing business models, as well as the amendments were made in national anti-money laundering and counter-terrorism financing (AML/CTF) legislation.

Accordingly, the regulatory environment in the area of money laundering prevention and counter terrorism financing has become considerably stricter and Latvian financial institutions had to continue to swiftly mitigate the risks associated with foreign customer service. Particular attention was paid to the so-called “shell arrangements”, that is the entities where entity is not related to any actual business activity and the activity of the entity creates little or no economic value.

After reviewing the business approach of previous years, Latvian banks have generally abandoned the segment of high-risk foreign customers and during the year actually completed the self-cleaning program. Consequently, in 2018 the share of foreign deposits in total deposits decreased by 37%. The decrease was partly offset by an increase of 7.2% in domestic customer deposits, which was in evidence alongside with the economic development of Latvia.

MTB improves risk management processes

Taking into account the common challenges facing the industry, the Bank's management implemented measures that included the termination of business relationships non-compliant with the risk policy and an increase in the number of local customers. In 2018, the share of Latvian and Lithuanian customer deposits in the Bank's deposit portfolio increased and reached 59%.

Improvement of the ML/TF risk management process was one of the priorities of the Bank's strategic development plan. The Bank has regularly conducted the identification, assessment and analysis of exposure to ML/TF risk, preventing significant risk increases. Following the changing regulatory environment, the Bank resorted to developing and improving ML/TF risk management methods in order to be in line with the set standards for ML/TF prevention and fully comply with the requirements of binding regulatory enactments. The Bank has improved the ML/TF and Sanctions risk management and risk control, which included the acquisition and launch of constantly updatable ACCUITY databases. In line with the new standards, the Bank also implemented a new multi-tier customer risk scoring system FICO Tonbeller (SIRON) and accordingly adjusted the Bank's working processes by introducing a multi-level customer approval system. It is of great significance that in 2018 the Bank implemented the recommendations made by Lewis Baach Kaufmann Middlemiss, an independent US consultancy company, and Exiger LLC, aiming to increase the efficiency of the ML/TF risk management internal control system.

Following the results of a review by the Financial and Capital Market Commission, in 2018 an administrative agreement was concluded between the Financial and Capital Market Commission and the Bank, imposing legal obligations and fines on the Bank. The fine imposed by FCMC was paid within the deadline specified in the decision and did not affect the Bank's day-to-day operations and servicing of customers.

In accordance with the administrative agreement, the Bank undertook to ensure independent reviews of the ML/TF risk management internal control system:

- 1) on the compliance of the customer base risk classification;
- 2) on the compliance of the IT software used in the ML/TF risk management;
- 3) on the compliance of the Bank's internal control system in the AML/CTF area.

The results of first two reviews and independent evaluations conducted by the certified auditors company Deloitte were received in the middle of 2018, along with the assessment and further recommendations for the improvement of the respective areas.

MANAGEMENT REPORT

By the end of 2018, the Bank implemented all the proposals and recommendations made in the course of the independent evaluation, improved the technical functions of the AML/CTF software, as well as implemented additional functionality and thoroughly documented the functionality of the customer risk scoring system. Until the end of 2018, the Bank also performed a compliance review and audit of all customers, which were subject to enhanced due diligence, persistently reducing the number of customers that could pose an excessive ML/TF risk.

Activity and financial performance of MTB

While implementing the Bank's transformation action plan, in December 2018 changes took place in the Bank's shareholders structure: a new minority shareholder joined the Bank. By promoting the strengthening of corporate governance, the new Council of the Bank was elected at the extraordinary shareholders' meeting on 10 December 2018, determining the date of 27 December 2018 as the date of commencement of the new Council's term of office. Jurijs Adamovičs, Ivars Grunte and Goča Tutberidze were elected to the Council of the Bank. The composition of the new Council of the Bank ensures an optimal combination of individual competencies and suitability of the elected candidates. J. Adamovičs is a competent and internationally recognised professional specialising in the fields of bank restructuring, business recovery and business transformation management, who is setting the preparation of the Bank for the attraction of a strategic investor as his key priority. The election of Mr. Grunte, the lead partner at TGS Baltics and a Member of the Latvian Collegium of Sworn Advocates, to the position of a member of the Council is a clear signal to the market players of the Bank's intent to strengthen its internal corporate governance process and to ensure the operation of the principle and system aimed at independent prevention of conflicts of interests. The key role of Mr. Tutberidze in the new Council is to ensure the succession of changes to be implemented within the restructuring plan of the Bank, monitoring of the management of specific risks pertaining to the Bank's operation and to demonstrate stability to the Bank's long-term partners and customers.

In the 2nd quarter of 2018, amendments were introduced in regulatory framework to prohibit servicing of the so-called "shell arrangements", where the entity is not related to any actual business activity and the activity of the entity creates little or no economic value. In line with these amendments, as well as following the implementation of the policy of ceasing business relationships with non-compliant customers, in 2018 the volume of the Bank's deposits decreased by 32%.

In 2018, the quality of the Bank's historical loan portfolio continued to deteriorate as a result of the Bank's credit policy implemented in previous years, which brought along a decline in interest income on issued loans. However, in the second half of 2018, there were taken steps to improve the Bank's internal control system in the area of credit risk management, which included joining of professionals in the field of credit restructuring and recovery to the Bank's team.

Regardless of the above-mentioned factors that had a considerable impact on the Bank's operations and performance, the Bank concluded the year 2018 with a profit of EUR 300 thousand, in comparison with the adjusted loss of EUR 7 900 thousand in 2017.

In 2018, the Bank continued to actively develop its payment card business. New payment card designs were highly appreciated and exhibited at the MasterCard Museum in Stockholm. In 2018, the Bank implemented contactless cards and started offering mini-POS terminals to the customers – legal entities, as well as replaced the POS terminal network with POS terminals for contactless cards.

Subsequent events

On 3 January 2019, the new Council elected Solvita Deglava to the position of the Chairman of the Board of the Bank, who had proven to be a top-level professional in the areas of business transformation management and finance. While continuing the process of changing the corporate governance of the Bank, on 21 February 2019, the Board elected Ruta Amtmane to the position of a member of the Board, whose responsibilities are legal and AML/CTF matters.

The new management of the Bank immediately expressed its strong uncompromising stance against money laundering and other activities that are not compliant with the international regulatory framework.

In May 2019, the Deputy Chairman of the Council Goča Tutberidze resigned. The Bank has initiated the process of electing a new Council. The shareholders of the Bank have been asked to submit proposals on nominees to the new Council, whose suitability thereafter will be assessed in accordance with the Bank's internal nominee assessment procedures and then will be further assessed by the Financial and Capital Market Commission.

MANAGEMENT REPORT


In 2019, the improvement of the ML/TF risk management process continued, within which an independent overall review of the Bank's internal control system was conducted. As a result of the review, a satisfactory opinion as well as separate recommendations for further improvement of the internal control system were received. In 2019, the Bank has already implemented almost all the recommendations given by the independent expert.

At the beginning of 2019, the Bank updated the strategy for future operations and worked out a detailed business plan for the period 2019-2021, which envisages the change of business model in the following directions:

- to perform the Bank's transformation into a mainly residents servicing credit institution during the year 2019;
- to actively resume conventional banking operations, primarily focusing on new lending to SME sector in Latvia and Lithuania;
- to strengthen the Bank's position as a niche banking services provider to SME sector in Latvia and Lithuania.

On behalf of the Council and the Board of the Bank:

Best regards,



Jurijs Adamovičs
Chairman of the Council



Solvita Deglava
Chairperson of the Board

5 July 2019

INFORMATION ON THE BANK'S MANAGEMENT

Council members as of the date of signing these financial statements

Name, surname	Position	Date of appointment
Jurijs Adamovičs	Chairman of the Council	28 December 2018
Ivars Grunte	Member of the Council	10 December 2018

In 2018 Natalija Prohorova and Valerijs Haliulins resigned from the Council.
In 2019 Goča Tutberidze resigned from the Council.

Board members as of the date of signing these financial statements

Name, surname	Position	Date of appointment
Solvita Deglava	Chairperson of the Board	03 January 2019
Ruta Amtmane	Member of the Board	21 February 2019
Jekaterina Meinharde	Member of the Board	05 December 2014

In 2018 Ivars Lapiņš and Sergejs Golubčikovs resigned from the Board.
In 2019 Dmitrijs Kozlovs and Ilze Pudiste resigned from the Board.

STATEMENT OF RESPONSIBILITY OF THE BANK'S MANAGEMENT

The management of AS Meridian Trade Bank is responsible for the preparation of the Bank's separate financial statements and the consolidated financial statements of the Bank and its subsidiary AS MTB Finance (hereinafter – the Group).

The financial statements presented on pages 8 to 82 are prepared based on source documents and present fairly the financial position of the Group and the Bank as at 31 December 2018 and the results of their operations, and cash flows for the year then ended.


The consolidated and the Bank's separate financial statements are prepared in accordance with the International Financial Reporting Standards, as adopted by the European Union. 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 a proper accounting system, safeguarding the Group's and the Bank's assets, and the detection and prevention of fraud and other irregularities in the Group and the Bank. Management is also responsible for operating the Group and the Bank in compliance with the Law on Credit Institutions, regulations of the Finance and Capital Market Commission and other legislation of the Republic of Latvia applicable to credit institutions.

On behalf of the Council and the Board of the Bank:



Juris Adamovičs
Chairman of the Council



Solvita Deglava
Chairperson of the Board

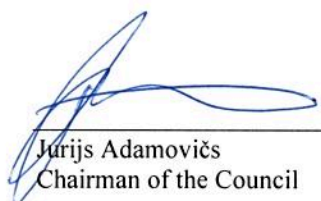
5 July 2019

BANK'S SEPARATE AND GROUP'S CONSOLIDATED STATEMENT OF FINANCIAL POSITION

ASSETS	Note	2018	2018	2017	2017	2016	2016
		Group	Bank	Group	Bank	Group	Bank
		EUR'000	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000
				(restated)	(restated)	(restated)	(restated)
Cash and balances due from the Bank of Latvia	6	86,559	86,559	107,313	107,313	74,470	74,470
Demand deposits with credit institutions	7	7,067	7,067	21,429	21,429	33,140	33,140
Held-to-maturity investments		-	-	6,356	6,356	16,962	16,962
Available for sale financial investments		-	-	32,481	32,481	53,285	53,285
Financial assets at amortised cost	8,9	4,000	4,000	-	-	-	-
Financial assets at fair value through other comprehensive income		344	344	-	-	-	-
Loans and receivables:		62,139	79,300	78,669	95,382	104,148	122,427
<i>Loans and term deposits due from credit institutions</i>	10	400	400	1,884	1,884	9,395	9,395
<i>Loans and advances to customers</i>	11	61,739	78,900	76,785	93,498	94,753	113,032
Intangible assets		9	9	28	28	-	-
Property and equipment	12	764	758	982	974	1,111	1,109
Investment properties	13	15,807	-	15,196	-	15,910	-
Other assets	14	6,717	4,811	8,403	6,043	3,912	1,785
Total assets		183,406	182,848	270,857	270,006	302,938	303,178
LIABILITIES AND EQUITY							
Financial liabilities at amortised cost:		171,952	171,956	254,805	254,807	276,732	276,732
<i>Deposits</i>	15	168,554	168,558	249,422	249,424	270,118	270,118
<i>Subordinated liabilities</i>	16	3,398	3,398	5,383	5,383	6,614	6,614
Other liabilities	17	2,697	2,482	5,604	5,356	10,470	9,778
Provisions		53	53	-	-	-	-
Total liabilities		174,702	174,491	260,409	260,163	287,202	286,510
Shareholders' equity							
Share capital	18	16,598	16,598	16,598	16,598	15,651	15,651
Share premium		260	260	260	260	260	260
Reserve capital	18	4,155	4,155	4,155	4,155	4,155	4,155
Fair value reserve		141	141	35	35	(93)	(93)
Accumulated losses		(12,450)	(12,797)	(10,600)	(11,205)	(4,237)	(3,305)
Total Shareholders' equity		8,704	8,357	10,448	9,843	15,736	16,668
Total liabilities and equity		183,406	182,848	270,857	270,006	302,938	303,178

The accompanying notes on pages 12 to 82 form an integral part of these Bank separate and Group consolidated financial statements.

The Council and the Board of the Bank approved the issue of these Bank separate and Group consolidated financial statements as presented on pages 8 to 82 on 5 July 2019.


Jurijs Adamovičs
Chairman of the Council


Sólvița Deglava
Chairperson of the Board

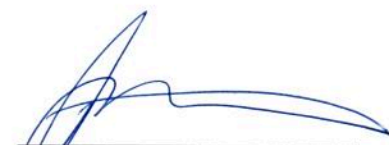
5 July 2019


BANK'S SEPARATE AND GROUP'S CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

	Note	2018 Group EUR'000	2018 Bank EUR'000	2017 Group EUR'000 (restated)	2017 Bank EUR'000 (restated)
Interest income	19	2,506	2,483	3,922	4,020
<i>including income at effective interest rate</i>		2,243	2,243	3,922	4,020
Interest expenses	20	(1,542)	(1,542)	(1,587)	(1,587)
Net interest income		964	941	2,335	2,433
Commission and fee income	21	10,077	10,074	6,653	6,651
Commission and fee expense	22	(2,263)	(2,263)	(2,066)	(2,066)
Net commission income		7,814	7,811	4,587	4,585
Gain on trading with financial instruments, net	23	2,116	2,476	2,653	2,645
Other operating income		591	156	1,210	38
Other operating expenses		(466)	(140)	(1,642)	(125)
Net operating income		11,019	11,244	9,143	9,576
Administrative expenses	24	(8,437)	(8,278)	(10,066)	(9,891)
Net impairment allowance expense	11,13	(2,539)	(2,665)	(5,440)	(7,585)
Profit/(loss) before tax		43	301	(6,363)	(7,900)
Income tax expenses	25	(1)	(1)	-	-
Profit(loss) for the reporting period		42	300	(6,363)	(7,900)
Other comprehensive income					
<i>Items that could be reclassified to profit or loss</i>					
Net gains on financial assets measured at FVOCI		106	106	128	128
Other comprehensive income for the reporting year		106	106	128	128
Total comprehensive income/ (loss)		148	406	(6,235)	(7,772)

The accompanying notes on pages 12 to 82 form an integral part of these Bank separate and Group consolidated financial statements.

The Council and the Board of the Bank approved the issue of these Bank separate and Group consolidated financial statements as presented on pages 8 to 82 on 5 July 2019.


Juris Adamovičs
Chairman of the Council


Solvita Deglava
Chairperson of the Board

5 July 2019


BANK'S SEPARATE AND GROUP'S CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

Group EUR'000	Share capital	Share premium	Reserve capital	Fair value reserve	Retained earnings	Total equity
As at 31 December 2016 (restated)	15,651	260	4,155	(93)	(4,237)	15,736
Increase in share capital	947	-	-	-	-	947
Loss for the reporting period	-	-	-	-	(6,363)	(6,363)
Other comprehensive income	-	-	-	128	-	128
Total comprehensive income/ (loss)	-	-	-	128	(6,363)	(6,235)
As at 31 December 2017 (restated)	16,598	260	4,155	35	(10,600)	10,448
IFRS 9 implementation impact	-	-	-	-	(1,892)	(1,892)
Restated balance as at 1 January 2018	16,598	260	4,155	35	(12,492)	8,556
Profit for the reporting period	-	-	-	-	42	42
Other comprehensive income	-	-	-	106	-	106
Total comprehensive income/ (loss)	-	-	-	106	42	148
As at 31 December 2018	16,598	260	4,155	141	(12,450)	8,704

Bank EUR'000	Share capital	Share premium	Reserve capital	Fair value reserve	Retained earnings	Total equity
As at 31 December 2016 (restated)	15,651	260	4,155	(93)	(3,305)	16,668
Increase in share capital	947	-	-	-	-	947
Loss for the reporting period	-	-	-	-	(7,900)	(7,900)
Other comprehensive income	-	-	-	128	-	128
Total comprehensive income/ (loss)	-	-	-	128	(7,900)	(7,772)
As at 31 December 2017 (restated)	16,598	260	4,155	35	(11,205)	9,843
IFRS 9 implementation impact	-	-	-	-	(1,892)	(1,892)
Restated balance as at 1 January 2018	16,598	260	4,155	35	(13,097)	7,951
Profit for the reporting period	-	-	-	-	300	300
Other comprehensive income	-	-	-	106	-	106
Total comprehensive income/ (loss)	-	-	-	106	300	406
As at 31 December 2018	16,598	260	4,155	141	(12,797)	8,357

The accompanying notes on pages 12 to 82 form an integral part of these Bank separate and Group consolidated financial statements.

The Council and the Board of the Bank approved the issue of these Bank separate and Group consolidated financial statements as presented on pages 8 to 82 on 5 July 2019.


Juris Adamovičs
Chairman of the Council


Solvita Deglava
Chairperson of the Board

5 July 2019


BANK'S SEPARATE AND GROUP'S CONSOLIDATED STATEMENT OF CASH FLOWS

		2018	2018	2017	2017
		Group	Bank	Group (restated)	Bank (restated)
	Note	EUR'000	EUR'000	EUR'000	EUR'000
Cash flows from operating activities					
Profit/(loss) before corporate income tax		43	300	(6,363)	(7,900)
Depreciation		329	327	310	307
Increase of impairment allowance		2,603	2,613	5,440	7,585
Changes in the fair value of investment property		(125)	-	731	-
Other changes		107	107	128	128
Increase in cash and cash equivalents used in operating activities before changes in operating assets and liabilities		2,957	3,347	246	120
Due from credit institutions (term over 3 months)		309	309	97	97
Loans and advances to customers		10,566	8,739	13,029	12,449
Shares and other non-fixed income securities		(58)	(58)	(64)	(64)
Fixed income debt securities		34,550	34,550	31,475	31,475
Decrease /(increase) in other assets		1,670	2,588	(4,992)	(4,759)
Decrease in deposits		(80,869)	(80,867)	(20,695)	(20,694)
Decrease in other liabilities		(2,855)	(2,823)	(4,864)	(4,418)
Cash flows from operating activities		(33,730)	(34,215)	14,232	14,206
Cash flow from investing activities					
Purchased property and other equipment		(92)	(92)	(208)	(199)
Acquisition of investment property		(485)	-	(17)	-
Net cash flow from investing activities		(577)	(92)	(225)	(199)
Cash flows from financing activities					
Share issue		-	-	947	947
Decrease in subordinated liabilities		(1,985)	(1,985)	(1,231)	(1,231)
Cash flows from financing activities		(1,985)	(1,985)	(284)	(284)
Net (decrease)/ increase in cash and cash equivalents		(36,292)	(36,292)	13,723	13,723
Cash and cash equivalents at the beginning of the year		129,917	129,917	116,194	116,194
Cash and cash equivalents at the end of the year	26	93,625	93,625	129,917	129,917

The accompanying notes on pages 12 to 82 form an integral part of these Bank separate and Group consolidated financial statements.

The Council and the Board of the Bank approved the issue of these Bank separate and Group consolidated financial statements as presented on pages 8 to 82 on 5 July 2019.


Jurij Adamovičs
Chairman of the Council


Solvita Deglava
Chairperson of the Board

5 July 2019

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

1 GENERAL INFORMATION

Information on the Bank

AS Meridian Trade Bank (until 6 May 2014 AS SMP Bank) was incorporated in the Republic of Latvia as a joint stock company "Multibanka" in 1994, in Riga and is licensed as a bank offering a wide range of financial services to enterprises and individuals. The legal address of the Bank is Elizabetes iela 57, Riga, Latvia. The Bank has a branch in Liepaja, 7 cash offices in Riga, and a cash office in each Ventspils, Daugavpils, Olaine, Jelgava, Saulkrasti, Jūrmala and Krāslava. The Bank has a foreign branch in Vilnius (Lithuania) with local cash offices in Klaipeda and Kaunas. In February 2019 a representative office in Moscow (Russian Federation) was closed.

These financial statements include the Group consolidated and Bank separate financial statements. The consolidated financial statements for year ended 31 December 2018 include the financial statements of the Bank and its subsidiary AS MTB Finance (hereinafter - the Group). The legal address of the AS MTB Finance is Elizabetes iela 57, Riga, Latvia. AS MTB Finance manages real estate properties and provide lease services.

The financial statements were approved for issue by the Board on 5 July 2019. The shareholders have the right to reject these financial statements and request that new financial statements are prepared.

Legislation regulating the Bank's operations

The Bank's operations are governed by the law 'On Credit Institutions', 'Commercial Law' and regulations issued by the Financial and Capital Market Commission (the FCMC). The above regulations govern capital adequacy, minimum equity, liquidity, foreign exchange positions, risk transaction restrictions with respect to one counterparty, group of related customers and related parties of the Bank, as well as other applicable requirements.

2 BASIS OF PREPARATION

Statement of Compliance

These financial statements were prepared in accordance with the International Financial Reporting Standards as adopted by the EU (IFRS) on a going concern basis. The financial statements were prepared on a historical cost basis, except for financial assets and liabilities measured at fair value through other comprehensive income, that were disclosed at fair value.

After considering key risks the management believes that the going concern basis is appropriate for the preparation of these financial statements, however material uncertainty exists with regard to the going concern basis which is described in Note 40. The financial and capital position of the Group and its business activities, the objectives and policies of risk management and the key risks to which the Group is exposed are described in section 'Risk Management'. Liquidity risk management is particularly important with regard to the going concern basis as the inability to attract sufficient funds to honour payment liabilities may cause the Bank to borrow funds at excessive cost, breach regulatory requirements, delay regular settlements or make the Group no longer compliant with the going concern basis. For more information please refer to section 'Liquidity risk management'. Of equal importance to the Group's compliance with the going concern basis is compliance with regulatory requirements, in particular those relating to capital adequacy.

Business activities are planned and carried out by the Group in view of the available capital and in line with regulatory requirements. The capital adequacy calculation and wider disclosures on current and expected capital adequacy requirements are provided in section 'Capital management'. In addition to other risk policies and procedures the Group has a comprehensive liquidity risk management and capital planning framework in place.

The management of the Group and the Bank consistently monitors and evaluates the market situation and its potential impact on the Group and the Bank, if any. Based on the information available to date the management is certain that the measures implemented by the Bank are sufficient and appropriate and there is no material impact on the Bank's and the Group's operations at the reporting date nor is any expected in the future.

The preparation of financial statements under IFRS as adopted by the EU requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities and the reported income and expenses for the reporting period. Although such estimates are based on reasonable information available to management regarding these events and activities, actual results may differ from these estimates.

Basis of measurement

The financial statements are prepared on the historical cost basis except for the following:

- financial assets and liabilities at fair value through profit or loss are stated at fair value (including financial assets held for trading);
- financial assets at fair value through other comprehensive income are stated at fair value;

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

- investment property is carried at fair value.

Functional and Presentation Currency

All amounts in these financial statements are presented in thousands of euro (EUR'000), unless stated otherwise. Euro is the functional currency of the Group and the Bank.

3 SIGNIFICANT ACCOUNTING POLICIES

The following significant accounting policies have been applied in the preparation of the consolidated financial statements:

Basis for consolidation

Subsidiaries

Subsidiaries are entities controlled by the Group. The Group controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date on which control commences until the date on which control ceases.

The investment in AS MTB Finance, in which the Bank holds a 100% interest and voting rights, is accounted for in the Bank's separate financial statements at cost less impairment.

Transactions eliminated on consolidation

Intra-group transactions, balances and unrealised profits arising from intra-group transactions are eliminated in the course of consolidation. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

Loss of control

When the Group loses control over a subsidiary, it derecognises the assets and liabilities of the subsidiary, and any related NCI and other components of equity. Any resulting gain or loss is recognised in profit or loss. Any interest retained in a former subsidiary is measured by the Group at fair value when control is lost.

Currency translation

Foreign exchange transactions are translated into the respective functional currency at the reference exchange rate published by the European Central Bank on the date of the respective transaction.

Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated into the functional currency at the spot exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the period.

Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are translated into the functional currency at the spot exchange rate at the date of acquisition or the date that the fair value was determined, respectively. Foreign currency differences arising on translation are recognised in the profit and loss statement except for the differences arising on the translation of available-for-sale equity instruments or a financial liability designated as a hedging instrument in a hedge of the net investment in a foreign operation or in a qualifying cash flow hedge, which are recognised in other comprehensive income. Monetary assets and liabilities denominated in foreign currencies and carried at historical cost are translated into the functional currency at the spot exchange rate at the transaction date.

Foreign exchange gains or losses arising from a monetary item receivable from or payable to a foreign operation, the settlement of which is neither planned nor likely to occur in the foreseeable future and which in substance is considered to form part of the net investment in the foreign operation, are recognised in other comprehensive income and accumulated in the translation reserve.

The exchange rates for the most significant currencies as set by the European Central Bank at reporting date are as follows:

<i>Currency</i>	<i>Reporting date</i>	
	31.12.2018	31.12.2017
USD	1.1450	1.1993
RUB	79.7153	69.3920

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Financial instruments (policies applicable as from 1 January 2018)

Financial instruments are classified into the following categories:

Financial assets at fair value through profit or loss

Financial assets are measured at fair value through profit or loss if they are not measured at amortised cost or measured at fair value through other comprehensive income.

For equity instruments that would otherwise be measured at fair value through profit or loss, at initial recognition an irrevocable election may be made to recognise those at fair value through other comprehensive income. The option to choose is applicable to each instrument individually.

Interest on financial assets measured at fair value through profit or loss is included in net interest income. Revaluation and trading gains or losses arising from changes in the fair value of the respective financial assets are included directly in the income item "Net financial income". Such financial assets and liabilities after initial recognition are revalued at fair value based on available market prices or broker quoted prices.

Financial assets at amortised cost

In order to measure a financial asset at amortised cost, it should be held concurrently within a such business model that aims to hold a financial asset in order to receive its contractual cash flows and the contractual terms of the financial asset should give rise on specific dates to cash flows that are solely payments of principal and interest on the principal amount outstanding (SPPI principle). Financial assets measured at amortised cost are carried at amortised cost using the effective interest rate method, less any allowance for impairment.

A gain or loss on a financial asset that is measured at amortised cost is recognised in profit or loss when the financial asset is derecognised, reclassified through the amortisation process or in order to recognise impairment gains or losses. Financial assets at amortised cost are recognised on drawdown. From the date of signing of a relevant contract till drawdown they are accounted for as off-balance sheet commitments.

When amending or revising the contractual cash flows of financial assets that do not result in derecognition, the Group and the Bank shall recalculate the gross carrying amount of the financial assets and recognise revenue or expense from changes in the statement of income. The new gross carrying amount is recalculated by discounting the modified cash flows at the original effective interest rate (or credit-adjusted effective interest rate for purchased or originated credit-impaired financial assets). The new gross carrying amount is an estimate of the present value resulting from the initial effective interest rate of the financial asset or the credit-adjusted effective interest rate on a financial asset that is impaired or impaired by discounting the modified or revised contractual cash flows. Estimates of expected cash flows include all contractual cash flows and payments, except for expected credit losses, unless the financial asset is acquired or issued with impairment. Costs or commissions adjust the carrying amount of the modified financial asset and are amortised over the remaining period of repayment of the modified asset.

If financial assets cannot be recovered, they are written off and charged against allowance for credit losses. The management of the Group decides on writing-off of financial assets. Recoveries of loans previously written off are credited to the statement of income.

This category includes claims on credit institutions, loans and receivables and fixed income securities that correspond to the principle of "only principal and interest payments".

Liabilities at amortised cost

Liabilities at amortised cost include deposits and account balances of credit institutions, balances of customer current accounts and customer deposits, subordinated liabilities and other financial liabilities.

Financial liabilities at amortised cost are initially measured at fair value less direct transaction costs and subsequently measured at amortised cost using the effective interest rate method.

The fixed maturity of subordinated deposits is at least five years at the time of their creation and these deposits must be repaid before maturity only in the event of the cessation of business or bankruptcy of the Bank, when those ranked before the shareholders' claims. Likewise, issued subordinated debt securities must be repaid before maturity only in the event of the cessation of business or bankruptcy of the Bank, when they rank before the shareholders' claims.

Financial assets at fair value through other comprehensive income

For a financial asset to be measured at fair value through other comprehensive income, it should be concurrently held within a business model the aim thereof is both to receive contractual cash flows and to sell the financial asset and the contractual terms of the financial asset should give rise on specific dates to cash flows that are "solely payments of principal and interest on the principal amount outstanding". The Group's financial assets measured at fair value through

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

other comprehensive income are expected to be held for an indefinite period of time and may be sold if required by liquidity or changes in interest rates, exchange rates or share prices.

Financial assets measured at fair value through other comprehensive income are subsequently, after initial recognition, re-measured at fair value based on available market prices. A revaluation gain or loss on a financial asset measured at fair value through other comprehensive income is recognised in other comprehensive income, except for impairment gains or losses and foreign exchange gains and losses, until the financial asset is derecognised or reclassified. For debt securities the difference between the initial carrying amount and amortised cost determined by the effective interest rate method is treated as interest income; upon de-recognising of a security the cumulative fair value revaluation gain previously recognised in other comprehensive income is reclassified from equity to profit or loss.

For financial assets measured at fair value through profit or loss other than equity, provisions for impairment are recognised in other comprehensive income and do not reduce their carrying amount in the balance sheet. Provisions for impairment are recognised in the income statement.

For non-equity financial instruments measured at fair value through other comprehensive income, the loss allowance is recognised in other comprehensive income and does not reduce the carrying amount in the balance sheet. Provisions for impairment are recognised in profit or loss.

For equity instruments, that are not held for trading and not acquired as a result of business combinations, the Group and the Bank, upon initial recognition, should make an irrevocable election to present the subsequent changes in fair value of the instruments in other comprehensive income or in profit or loss. This election is made on an instrument-by-instrument basis. Amounts presented in other comprehensive income are not subsequently transferred to profit or loss, but cumulative gain or loss on disposal is transferred directly to retained earnings.

Dividends on equity instruments measured at fair value through other comprehensive income are recognised in profit or loss. Equity instruments are not assessed for impairment, but carried at fair value.

Recognition

All purchases and sales of financial assets that require delivery in accordance with accepted market principles ('ordinary' purchases and sales) are accounted for at the date of the transaction, which is the date on which the Group / the Bank commits to deliver the financial asset. Other purchases are recognised when the Group / the Bank becomes a party to the contractual terms of the instrument.

Measurement

A financial asset or liability is initially measured at fair value plus transaction costs that are directly attributable to the acquisition of a financial asset or liability if the financial asset or liability is not measured at fair value through profit or loss.

After initial recognition, financial assets are measured at fair value without deducting transaction costs that might arise in the event of a sale or exclusion.

Derecognition

Financial assets – write-off

Financial assets are written off in full or in part when the Group /the Bank has exhausted all practical possibilities of recovery and has concluded that there is no reason to believe that the amounts will be recovered. The write-off is a de-recognition event. The Group / the Bank may write off financial assets that are still subject to enforcement activity when the Group/ the Bank seeks to recover amounts that are due under contracts, however, there is no reason to believe that they will be recovered.

Financial assets – de-recognition

The Group / the Bank derecognises financial assets when:

- the assets are redeemed or the rights to cash flows from the assets expired or
- the Group / the Bank transfers the rights to the cash flows from the financial assets or enter into a relevant agreement, while

(i) transferring all material risks and rewards of ownership of the asset, or

(ii) neither transferring nor retaining all material risks and rewards inherent in the ownership of the asset, nor retaining control. Control is maintained if the other party to the transaction does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose additional restrictions on the sale transaction.

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Repurchase and reverse repurchase agreements

Securities sold under sale and repurchase ("repo") agreements are accounted for as secured financing transactions, with the securities retained in the balance sheet and the counterparty liability included in amounts payable under repo transactions. The difference between the sale and repurchase price represents the interest expense and is recognised in the statement of comprehensive income over the term of the repo agreement using the effective interest rate method.

Securities purchased under agreements to resell ("reverse repo") are recorded as amounts receivable under reverse repo transactions. The differences between the purchase and resale prices are treated as interest income and accrued over the term of the "reverse repo" agreement using the effective interest method.

If assets purchased under an agreement to resell are sold to third parties, the obligation to return securities is recorded as a trading liability and measured at fair value.

Derivatives

Derivative financial instruments including foreign exchange contracts, currency and interest rate swaps and other derivative financial instruments are initially recognised in the statement of financial position at their fair value. Attributable transaction costs are recognised in the profit and loss statement of the relevant period. Fair values are obtained from quoted market prices or discounted cash flow models, as appropriate. OTC derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

The Group and the Bank do not use hedge accounting.

Offsetting

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

Classification and measurement of the financial instruments under IFRS 39 before 01 January 2018:

Financial instruments are classified into the following categories:

Financial assets and liabilities at fair value through profit or loss are financial assets or liabilities that are acquired or incurred for the purpose of selling or repurchasing in the near term; or that are part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking; or that are derivative financial instruments (except for derivatives used for hedging purposes); or that are upon initial recognition designated by the entity as assets or liabilities at fair value through profit or loss.

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Group or the Bank have the positive intention and ability to hold to maturity, and which are not designated at fair value through profit or loss, or available for sale, or loans and receivables.

Available-for-sale instruments are those financial assets that are designated as available-for-sale and are not classified as loans and receivables, held-to-maturity instruments or financial instruments at fair value through profit or loss.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than (a) those that the Group or the Bank intends to sell immediately or in the short-term, (b) those that the Group or the Bank designates upon initial recognition as financial assets at fair value through profit or loss or as available for sale; or (c) those for which the holder may not recover substantially all of its initial investments, other than because of credit deterioration. Loans and receivables include fixed-term amounts due from credit institutions, loans and receivables from customers and other financial assets which comply with these classification criteria.

Liabilities carried at amortised cost include deposits and account balances from banks and current account balances and deposits from customers, subordinated liabilities and other financial liabilities.

Financial liabilities carried at amortised cost are initially measured at fair value less directly attributable transaction costs and are subsequently re-measured to amortised cost using the effective interest rate method.

Subordinated deposits have a fixed term of at least five years from the date of placement and they are repayable before maturity only in the event of the cessation of business or bankruptcy of the Bank and such deposits rank before shareholders' claims. Similarly, subordinated debt securities are repayable before maturity only in the event of termination of the Bank's operations or the Bank's bankruptcy and such deposits rank before shareholders' claims.

A financial asset or liability is initially measured at fair value plus, in the case of a financial asset or liability other than designed at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or liability.

Subsequent to initial recognition, financial assets are measured at their fair values, without any deduction for transaction costs that may be incurred on sale or other disposal, except for:

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

- held-to-maturity investments and loans and receivables that are measured at amortised cost using the effective interest rate method; and
- investments in equity instruments that do not have a quoted market price in an active market and the Bank measures the fair value by using one of the valuation methods. The valuation methods include the latest information on market transactions consistent with the terms of transactions between informed and interested parties (if any); using the present fair value of another financial instrument that is substantially the same; using discounted cash flow analysis and option pricing models.
- a gain or loss on an available-for-sale financial asset is recognised in other comprehensive income (except for impairment losses and foreign exchange gains and losses on debt financial instruments) until the asset is derecognised, at which time the cumulative gain or loss previously recognised in equity is recognised in the income statement. Interest on an available-for-sale financial asset is recognised in the income statement using the effective interest rate method.

All financial liabilities, other than those designated at fair value through profit or loss and financial liabilities that arise when a transfer of a financial asset carried at fair value does not qualify for derecognition, are measured at amortised cost. Amortised cost is calculated using the effective interest rate method.

Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortised based on the effective interest rate of the instrument. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability.

When calculating the effective interest rate, the Group and the Bank estimate future cash flows considering all contractual terms of the financial instrument but not future credit losses.

Property and equipment

Items of property and equipment are measured at cost less accumulated depreciation and impairment losses.

Where an item of property, plant and equipment comprises major components having different useful lives, they are accounted for as separate items of property, plant and equipment. Cost includes expenses that are directly attributable to the acquisition of the asset.

Depreciation is charged to the profit and loss statement on a straight-line basis over the estimated useful lives of the individual assets. Depreciation commences on the date when the asset becomes available for use or, in respect of internally constructed assets, from the time an asset is completed and ready for use. Depreciation methods, useful lives and residual values are assessed annually. The annual depreciation rates are as follows:

Buildings	5%
Furniture and cars	20%
Computers	35%
Other fixed assets	20%

Intangible assets

Intangible assets acquired by the Group or the Bank are stated at cost less accumulated amortisation and impairment losses.

Software licences are capitalised on the basis of the costs incurred to acquire and customise the specific software. Depreciation is charged to the profit and loss statement on a straight-line basis over the estimated useful lives of the individual assets. The estimated useful lives are 5 to 7 years.

Repossessed assets

As part of the normal course of business the Group and Bank occasionally take possession of property that originally was pledged as security for a loan. When the Group and Bank acquire (i.e. gains a full title to) a property in this way, the property's classification follows the nature of its intended use by the Group and Bank. When the Group and the Bank are uncertain of their intentions with respect to property that they have repossessed, those properties are classified as investment property. Other types of collateral (repossessed finance lease objects) are classified as other assets and carried at cost net of impairment loss.

Investment property

Investment property is property held either to earn rental income or for capital appreciation or for both, but not for sale in the ordinary course of business or for administrative purposes. All investment properties are carried at fair value through profit and loss. The fair value of investment property is based on a valuation by an independent appraiser who holds a recognised and relevant professional qualification and has recent experience in the location and category of the investment property being valued. The fair value of the Group's investment property is measured by independent appraisers on a regular basis.

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Recognition of income and expenses

All significant categories of income and expenses are recognised on an accrual basis.

Interest income is recognised as it accrues in the profit and loss statement using the effective interest method. Interest income and expense include the amortisation of any discount or premium or other differences between the initial carrying amount of an interest bearing instrument and its amount at maturity calculated on an effective interest rate basis.

Loan origination fees and other fees including the related direct costs that are considered an integral part of the total loan profitability are deferred and amortised to the interest income over the estimated life of the financial instrument using the effective interest rate method.

Other fees, commissions and other income and expense items are recognised when the corresponding service has been provided.

Fair value measurement principles

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal, or in its absence, the most advantageous market to which the Group has access at that date. The fair value of liabilities represents the risk of default.

A number of the Group's accounting policies and disclosures require the determination of fair value for both financial and non-financial assets and liabilities carried at fair value or disclosures on their fair value should be made in the financial statements.

The Group and the Bank have an established control framework with respect to the measurement of fair values. This includes a valuation team that has overall responsibility for overseeing all significant fair value measurements, including Level 3 fair values.

Specific controls include:

- Verification of observable pricing;
- Re-performance of model valuations;
- A review and approval process for new models against observed market transactions;
- Analysis and investigation of significant daily valuation movements;
- Review of significant unobservable inputs, valuation adjustments and significant changes to the fair value measurement of Level 3 instruments compared to previous month.

The methods described below have been used for the determination of fair values.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price, i.e., the fair value of the consideration given or received, unless the fair value of that instrument is evidenced by comparison with other observable current market transactions with the same instrument (i.e., without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When transaction price provides the best evidence of fair value at initial recognition, the financial instrument is initially measured at the transaction price and any difference between this price and the value initially obtained from a valuation model is subsequently recognised in the profit and loss statement depending on the individual facts and circumstances of the transaction but not later than when the valuation is supported wholly by observable market data or the transaction is closed out.

When available, the Group and the Bank measure the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If a market for a financial instrument is not active, the fair value is established by the Group and the Bank using a valuation technique. Valuation techniques include recent arm's length transactions between knowledgeable, willing parties (if available), reference to the current fair value of other instruments that are substantially the same, discounted cash flow analyses and option pricing models. The chosen valuation technique should make maximum use of market inputs, rely as little as possible on estimates specific to the Group and the Bank, incorporate all factors that market participants would consider in setting a price, and be consistent with accepted economic methodologies for pricing financial instruments. Inputs to valuation techniques reasonably represent market expectations and measures of the risk-return factors inherent in the financial instrument. The Group and the Bank calibrate valuation techniques and test them for validity using prices from observable current market transactions in the same instrument or based on other available observable market data.

Where third-party information, such as broker quotes or pricing services, are used to measure fair value, the Group and the Bank assess and document the evidence obtained from the third parties to support the conclusion that such valuations meet the requirements of IFRS. This includes:

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

- Verifying that equity broker or pricing service is approved by the Group and the Bank for use in pricing the relevant type of financial instrument;
- Understanding how the fair value has been arrived at and the extent to which it represents actual market transactions;
- When prices for similar instruments are used to measure fair value, how these prices have been adjusted to reflect the characteristics of the instrument subject to measurement;

In determining the fair value of assets or liabilities the Group and the Bank use observable market data to the extent possible. Fair value is classified into different levels of the fair value hierarchy based on the inputs used in the measurement techniques:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

If the inputs used to measure the fair value of an asset or a liability might be categorised in different levels of the fair value hierarchy, the fair value measurement is categorised in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement.

The Group and the Bank recognise transfers between levels of the fair value hierarchy at the end of the reporting period during which the change has occurred. For further analysis of the basis for fair value refer to Note 38.

Impairment losses (policies applicable as from 1 January 2018)

The Group and the Bank have adopted IFRS 9 as issued by the IASB in July 2014 with a date of transition of 1 January 2018, which resulted in changes in accounting policies and adjustments to the amounts previously recognised in the financial statements. The Group and the Bank did not adopt any of IFRS 9 provision in previous periods. As permitted by the transitional provisions of IFRS 9, the Group and the Bank elected not to restate comparative figures. Any adjustment to the carrying amounts of financial assets and liabilities at the date of transition were recognised in the opening retained earnings of the current period.

Consequently, for notes disclosures, the consequential amendments to IFRS 7 disclosures have also only been applied to the current period. The comparative period notes disclosures repeat those disclosures made in the prior year.

Financial assets

Impairment requirements as laid out in IFRS 9 are applicable to the following financial instruments:

- financial assets at amortised cost;
- financial assets at fair value through other comprehensive income;
- loan commitments and financial guarantees.

The Management of the Group and the Bank considers both specific exposures and portfolio-level risks in determining the balance of impairment allowance for expected credit losses. The expected credit loss assessment is forward-looking and is based on unbiased and probability-weighted information about past events, current conditions and forecasts of future economic conditions. Impairment allowance for expected credit losses is recognised even if no credit loss event has happened. A loan or portfolio of loans is impaired and impairment losses are incurred if, and only if, there is objective evidence that the estimated present value of future cash flows is less than the current carrying value of the loan or portfolio of loans, and it can be reliably estimated.

For off-balance contingent liabilities, allowances for expected future losses are recognised as provisions. The provisioning principles for expected losses arising from off-balance sheet financial commitments and contingent liabilities are consistent with the principles and methods applied for on-balance sheet exposures. Additional considerations are applied to adjustments for expected conversion and future use patterns of the committed limits as well as the Group's performance in timely identification and termination of limits for deteriorating exposures.

The Group and the Bank have grouped the loans into 3 stages, based on the applied impairment methodology, as described below:

Stage 1 – performing loans: when loans are first recognised, the Group and the Bank recognise an allowance based on twelve months expected credit losses.

Stage 2 – loans with significant increase in credit risk: when a loan shows a significant increase in credit risk since initial recognition, the Group and the Bank record an allowance for the lifetime expected credit loss. The Group and the Bank use the following criteria to determine a significant increase in credit risk: contractual payments are overdue by more than

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

30 days, the loan is included in the watch list, the value of the collateral is lower than the carrying amount of the loan, a negative outlook for the industry.

Stage 3 – impaired loans with objective evidence of impairment. The Group and the Bank recognise lifetime expected credit losses for these loans and, in addition, accrue interest income on the amortised cost of the loan net of allowances. Provisions for impairment losses on individual loans are calculated according to the present value of their discounted future cash flows, however, the collateral value is adjusted to reflect the amount expected to be earned from the collateral. The definition of 'default' as used by the Group and the Bank to classify financial assets into Stage 3 does not differ from the one provided in Article 178 of Regulation 575/2013, i.e. exposure delayed 90 and more days (less days for some products), significant restructuring, insolvency or bankruptcy, or similar legal proceedings started or other indicators of unlikelihood to pay. Evidence that a financial asset is credit-impaired includes the following observable data:

- significant financial difficulty of the borrower;
- a breach of contract, such as a default or delinquency in interest or principal payments;
- granting to the borrower, for economic or contractual reasons relating to the borrower's financial difficulty, a concession that the Bank or the Group would not otherwise consider;
- the borrower entering bankruptcy or other financial reorganisation becomes highly probable;
- the purchase or origination of a financial asset at a deep discount that reflects the incurred credit losses;
- a combination of several other events that cause a loan to become credit-impaired.

In order to adapt the expected credit loss model, the Bank has applied it along with the existing model since mid-2017.

The Group and the Bank recognise impairment for FVOCI debt securities as applicable, depending on whether they are classified as Stage 1, 2 or 3, as explained above. However, in this event the expected credit losses will not reduce the carrying amount of these financial assets in the financial statement, which shall remain to be stated at fair value. Instead, an amount equal to the allowance that would arise if the assets were measured at amortised cost will be recognised in other comprehensive income as an accumulated impairment amount, with a corresponding charge to profit or loss.

For FVOCI debt securities considered to be 'low risk', the Group and the Bank apply a policy which assumes that the credit risk on the instrument has not increased significantly since initial recognition. Such instruments will include trade, investment grade securities where the borrower has strong capacity to meet its contractual cash flow obligations in the near term and adverse changes in economic and business conditions in the longer term may, but will not necessarily, reduce the ability of the borrower to fulfil its contractual cash flow obligations. For 'low risk' assets ECL is calculated as explained in Stage 1 above.

When estimating lifetime ECLs for undrawn loan commitments, the Group and the Bank:

a) estimate the expected portion of the loan commitment that will be drawn down over the expected life of the loan commitment, and b) calculate the present value of cash shortfalls between the contractual cash flows that are due to the Group and the Bank and the cash flows the Group and the Bank expect to receive for that expected portion of the loan drawn down.

For financial guarantee contracts, the Group and the Bank calculate the lifetime of ECLs based on the present value of the expected payments to reimburse the holder for a credit loss that it incurs less any amounts that the guarantor expects to receive from the holder, the debtor or any other party.

For revolving facilities such as credit cards and overdrafts, the Group and the Bank measure ECLs by determining the period over which they expect to be exposed to credit risk, taking into account the credit risk management actions that they expect to take once the credit risk has increased and that serve to mitigate losses.

Following a decrease in credit risk, a financial asset may be re-classified from Stage 3 to Stage 2 or from Stage 2 to Stage 1. The Group and the Bank use a sufficiently long (in some events – up to 2 years) probation period since all factors of enhanced risk or default do not exist any more, to establish a possibility to move a financial asset from Stage 3 to Stage 2 and from Stage 2 to Stage 1.

Expected credit loss will be determined by the Group and the Bank using the so-called EAD x PD x LGD method, where EAD is exposure at default, PD is probability of default and LGD is loss given default. The main macroeconomic and industry factors taken into account are gross domestic product, inflation rate and unemployment rate, real estate prices. For measurement of expected credit losses financial instruments are grouped on the basis of similar probability of default and common credit peculiarities.

As part of the portfolio based EAD x PD x LGD method each component is determined separately and then all components are aggregated on the portfolio level. PD evaluation is made by the Bank using migration matrices based on historical performance of portfolio of financial assets adjusted for forward-looking forecasts. EAD evaluation is made by the Group and the Bank using payment schedules adjusted, where necessary, for advance payments and taking into account off-balance sheet transactions.

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Model validation includes reviews of input data, underlying assumptions used for expected credit loss evaluation, and review of model output data. Back-testing is performed by testing whether the Stage 2 indicators correctly reflect an increase in credit risk, and namely, the Bank analyses the number and amount of cases when a loan is reclassified directly from Stage 1 to Stage 3, as well as it is intended to compare the actual historical performance of portfolio to the expected credit loss estimation results as per developed models.

The Group and the Bank first assess whether objective evidence of impairment exists individually for loans that are individually significant, and individually or collectively for loans that are not individually significant. If the Group and the Bank determine that no objective evidence of impairment exists for an individually assessed loan, whether significant or not, it includes that loan in a group of loans with similar credit risk characteristics and collectively assess them for impairment. As soon as information is available that specifically identifies losses on individually impaired loans included in a group of loans with similar credit risk characteristics, those loans are removed from the group. Assets that are individually assessed for impairment or for which an impairment loss is already recognised, are excluded from the total financial assets group tested to identify the risk of impairment.

The assessment of whether lifetime expected credit losses should be recognised is based on significant increases in the likelihood (Stage 2) or risk of a default (Stage 3) occurring since initial recognition instead of on evidence of a financial asset being credit-impaired at the reporting date or an actual default occurring. In most cases, there will be a significant increase in credit risk before a financial asset becomes credit-impaired or an actual default occurs (Stage 3), thus default (Stage 3) and credit-impaired loan classification will be closely aligned and will indicate non-performance of the borrower or significance of forbearance measures undertaken, but classification will not necessarily equal in all cases.

For individually assessed loans, the amount of impairment loss is measured as the difference between the loan's carrying amount and the present value of estimated future cash flows discounted at the loan's original effective interest rate. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. The calculation of the present value of the estimated future cash flows of a collateralised loan reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable. The amount of the loss is recognised in the statement of income.

If, in a subsequent period, the amount of the impairment loss decreases, the previously recognised impairment loss is reversed. Any subsequent reversal of the impairment loss is recognised in the statement of income, to the extent that the carrying value of the loan does not exceed what its amortised cost would have been absent the impairment at the reversal date. When a borrower fails to make a contractual payment of interest or principal due, but the Group believes that impairment is not appropriate on the basis of the level of collateral available or the stage of collections of amounts owed to the Group, the carrying amount of the loan is classified as past due but not impaired.

For purchased or originated credit-impaired financial assets, expected credit losses are discounted using the credit-adjusted effective interest rate determined at initial recognition. For purchased or originated credit-impaired financial assets only the cumulative changes in lifetime expected credit losses since initial recognition are recognised as a loss allowance.

Favourable changes in lifetime expected credit losses are recognised as an impairment gain, even if the lifetime expected credit losses are less than the amount of expected credit losses that were included in the estimated cash flows on initial recognition.

Fully impaired loans, the recovery of which may become economically unviable, may be written-off and charged against impairment allowance. They are not written-off until the necessary legal procedures have been completed and the amount of the loss is determined. When a loan or receivable is written-off, the claim against the borrower normally is not forgiven. Subsequent recoveries of amounts previously written-off are reported in the statement of income as recovered written-off assets within net credit losses on financial instruments.

For unused credits that have been granted, under the terms of the credit agreement, but not used, a conversion factor is calculated, which depends on historical data on the use of credit limits for the past 3 years. The unused credit amount is multiplied by the conversion factor and added to the loan balance.

Similarly as for loans to customers, the Group and the Bank estimate expected credit losses to reflect changes in credit risk since initial recognition of debt securities, loans to credit institutions and central banks exposures and commitments to extend credit. Impairment allowances are recognised based on forward looking information, even if no credit loss event has happened. The assessment considers broad range of information, but as most of these types of exposures are rated, it relies heavily on external credit ratings and rating agencies' reported default rates derived by calculating multi-period rating transition matrices. The LGD depends on the type of issuer (counterparty) and the external credit rating. Discounted cash flow is used to calculate EAD. The effective interest rate on debt securities is the yield at the time of purchase. The effective interest rate on a money market transaction is the interest rate of the transaction. Expected losses for balances in correspondent accounts and interbank overnight loans are not calculated due to the short-term nature of transactions (not exceeding one day).

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

If no credit rating is assigned, then the country's long-term credit rating is used, downgraded by 1 rating notch. Impairment provisions apply to financial assets measured at amortised cost but does not apply to financial assets measured at fair value through profit or loss. The Group and the Bank will recognise impairment for FVOCI debt securities, depending on whether they are classified as Stage 1, 2, or 3, as described above. The expected credit losses will not reduce the carrying amount of these financial assets in the statement on financial position, which remains at fair value.

For financial assets measured at fair value through other comprehensive income, the loss allowances are recognised in other comprehensive income and does not reduce their carrying amount in the balance sheet.

Non financial assets

The carrying amounts of the Group's and Bank's non-financial assets, other than deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated.

An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other assets and groups. The main assets and cash generating units considered by the Group comprise investment properties. Certain properties are valued on an individual basis and some others in aggregate as cash generating units – development projects. Impairment losses are recognised as profit or loss in the profit and loss statement. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

The recoverable amount of an asset or cash generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

In respect of other assets, except goodwill, impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the carrying amount of the asset does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Impairment losses under IAS 39 before 1 January 2018

At each reporting date the Group assesses whether there is objective evidence that the financial assets other than carried at fair value through profit or loss are impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

Objective evidence that financial assets (including equity securities) are impaired can include default or delinquency by a borrower, restructuring of a loan or advance by the Group on terms that the Group would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group. In addition, for an investment in an equity security, a significant or prolonged decline in its fair value below its cost is objective evidence of impairment.

The Group and Bank consider evidence of impairment for loans and advances and held-to-maturity investment securities at specific asset level. All loans and receivables from customers and held-to-maturity investment securities are assessed for specific impairment.

Impairment losses on assets carried at amortised cost are measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognised in the profit and loss statement and reflected in an allowance account against loans and receivables. Interest on the impaired asset continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through the profit and loss statement.

Impairment losses on available-for-sale investment securities are recognised by transferring the cumulative loss that has been recognised through other comprehensive income in equity to profit or loss. The cumulative loss that is removed from equity and recognised in profit or loss is the difference between the acquisition cost, net of any principal repayment and amortisation, and the current fair value, less any impairment loss previously recognised in statement of comprehensive income. Changes in impairment allowance attributable to time value are reflected as a component of interest income.

If, in a subsequent period, the fair value of an impaired available for sale bond increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in income statement, the impairment loss is

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

reversed, with the amount of the reversal recognised in income statement. However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognised in other comprehensive income.

Impact from adoption of IFRS 9 on carrying amount by class of financial instruments:

Group EUR'000	Cash, balances at central banks and credit institutions	Debt securities		Loans to public	Equity and other financial instruments		Off-balance sheet less provisions
According to IAS 39 as at 31 December 2017							
Measurement category*	LaR	HTM	AFS	LaR	FVPL and HFT	AFS	-
Carrying amount	130,627	6,356	32,195	76,784	3	283	5,110
IFRS 9 initial implementation impact:							
Expected credit losses	-	-	-	(1,662)	-	-	(230)
According to IFRS 9 as at 1 January 2018							
Measurement category**	AmC	AmC	FVOCI	AmC	FVPL	FVOCI	-
Carrying amount	130,627	6,356	32,195	75,122	3	283	4,880

* IAS 39 measurement category abbreviations: LaR – loans and receivables, FVPL – at fair value through profit or loss, HTM – held to maturity, AFS – available for sale, HFT – held for trading.

** IFRS 9 measurement category abbreviations: AmC – at amortised cost, FVPL – at fair value through profit or loss, FVOCI – at fair value through other comprehensive income.

Bank EUR'000	Cash, balances at central banks and credit institutions	Debt securities		Loans to public	Equity and other financial instruments		Off-balance sheet less provisions
According to IAS 39 as at 31 December 2017							
Measurement category*	LaR	HTM	AFS	LaR	FVPL and HFT	AFS	-
Carrying amount	130,626	6,356	32,195	93,498	3	283	5,110
IFRS 9 initial implementation impact:							
Expected credit losses	-	-	-	(1,662)	-	-	(230)
According to IFRS 9 as at 1 January 2018							
Measurement category**	AmC	AmC	FVOCI	AmC	FVPL	FVOCI	-
Carrying amount	130,626	6,356	32,195	91,836	3	283	4,880

The impact of the reversal of existing allowances and recognition of a new impairment allowance for loans and receivables according to IFRS 9 is a net increase in allowances by 1,892 thousand euros for the Group and the Bank. The increase is primarily connected with loans. It decreases capital and reserves. In order to reduce the negative impact of implementation of IFRS 9 on the capital ratios of the Group and the Bank, for the purposes of capital adequacy calculation the Group and the Bank use the 5-year transition period provided under the Regulation (EU) 2017/2395 (of 12 December 2017) concerning the impact of IFRS 9 on equity (CET1). During 2018, it is permitted to charge 95% of the allowance for expected loss back to equity. In planning their future operations, the Group and the Bank take account of the implementation impact of IFRS 9 and foresee measures to be taken to reduce the negative impact as described in Note 40.

Loan commitments

In the normal course of business, the Group and the Bank enter into credit related commitments comprising irrevocable credit line facilities, letters of credit and guarantees, and provides other forms of credit insurance.

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Financial guarantees are contracts that require the Group and the Bank to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument.

A financial guarantee liability is recognised initially at fair value net of associated transaction costs, and is measured subsequently at the higher of the amount initially recognised less cumulative amortisation or the amount of provision for losses under the guarantee. Provisions for losses under financial guarantees and other credit related commitments are recognised when losses are considered probable and can be measured reliably. For unused credit amounts that have been granted but not used in accordance with the terms of the loan agreement, a conversion factor is calculated, depending on the historical use of the credit limits over the last 3 years. The amount of unused credit is multiplied by the conversion factor and added to the loan balance. For the purpose of calculating EAD for unused loans, it is assumed that the unused credits will be repaid in accordance with the repayment schedule of the relevant loan agreement.

Financial guarantee liabilities and provisions for other credit related commitments are included within other liabilities.

Taxation

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date and any adjustment to tax payable in respect of previous years. Current corporate income tax assets and liabilities are measured at the amount expected to be obtained from or paid to tax authorities. Several Group companies pay income tax upon profit distribution (e.g. dividends). Beginning with 2018, the Bank and the Latvian Group subsidiaries are required to pay income tax on distributed profits. Correspondingly, with regards to Group companies registered in these jurisdictions, income tax on profit distribution is recognised as expense at the moment dividends are declared. Deferred income tax is provided using the balance sheet liability method for tax loss carry forwards and temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. In accordance with the initial recognition exception, deferred tax is not initially recognised for assets or liabilities in a transaction that is not a business combination, if the transaction during its initial recognition affects neither accounting nor taxable profit. Deferred tax liabilities are not recognised for the temporary differences arising on the initial recognition of goodwill and for the part of goodwill that is not deductible for tax purposes. Deferred income tax is determined based on tax rates set as at the balance sheet date and expected to be effective when the temporary differences reverse or tax loss carried forward are utilised. Deferred tax is calculated using the rate applicable to retained earnings until the decision is made on profit distribution. As a result, in jurisdictions where income tax is payable on distributed profit (such as dividends) deferred tax asset or liabilities are recognised using the tax rate applicable to retained earnings. Deferred tax assets and liabilities are netted only within the individual companies of the Group and only if certain criteria are met. Deferred tax assets for deductible temporary differences and tax loss carry forwards are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilised. The carrying amount of deferred tax asset, if any, is reviewed at each reporting date and reduced to the extent it matches taxable income that could be generated in the future and used against. The future taxable profits and the amount of tax benefits that are probable in the future are based on a medium term financial forecast prepared by management and extrapolated results thereafter. The financial forecast is based on management expectations that are believed to be reasonable under the circumstances.

Cash and Cash Equivalents

Cash and cash equivalents include notes and coins on hand, unrestricted balances held with the Bank of Latvia and highly liquid financial assets with original maturities of less than three months, which are subject to insignificant risk of changes in their fair value, and are used by the Group and the Bank in the management of its short-term commitments, less amounts due to the Bank of Latvia and credit institutions with maturities of less than 3 months.

In accordance with IFRS 9, cash and cash equivalents and demand deposits with credit institutions include financial assets that are carried at amortised cost and are subject to impairment. When making the calculations, the Group and the Bank found out that the risk of default is not significant, therefore, provisions for impairment are not necessary and are not included in these financial statements.

Leases

Classification

Only risks and rewards incidental to ownership of the leased asset during the lease period should be considered in determining the classification of lease. Relevant risks include the possibility of losses from idle capacity or technological obsolescence and from decreases in the value of the asset; relevant rewards may include the gain from the increase in value of the asset or realization of the residual value at the end of the lease. Conversely, risks associated with construction of the asset prior to lease commencement, financing such construction and the costs of providing services using the leased asset, are not incidental to ownership of the leased asset during the lease period and in the Management's view generally

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

should be disregarded in determining the classification of the lease. The classification of a lease is determined at the inception of the lease and is not revised unless the lease agreement is modified.

Finance lease

A finance lease is lease that transfers substantially all the risks and rewards incidental to ownership of an asset. Title may or may not eventually be transferred.

When assets are leased out under finance lease terms, the net investment in finance lease is recognised as a receivable. The net investment in finance lease represents the difference between the gross receivable and the unearned finance income.

Operating lease

An operating lease is a lease other than a finance lease.

Assets leased out under an operating lease are presented within property and equipment in the statement of financial position net of accumulated depreciation. They are depreciated over their expected useful lives on a basis consistent with similar owned Property and equipment.

Provisions

A provision is recognised in the statement of financial position when the Group and Bank has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

A provision for restructuring is recognised when the Group and the Bank has approved a detailed and formal restructuring plan, and the restructuring either has commenced or has been announced publicly. Future operating costs are not provided for.

Dividends

The Group and the Bank receive dividends from the equity instruments that are recorded to income when the right to receive payment is established.

Proposed dividends are recognised in the financial statements only when approved by the shareholders.

Employee benefits

Short term employee benefits, including salaries and social security contributions, bonuses and vacation benefits are included in net operation expenses on an accrual bases. The Group and the Bank pay fixed security contributions to the State Social Fund on behalf of its employees during the employment period in accordance with local legal requirements and the Group and Bank will have no obligations to pay further contributions relating to employee services in respect to pension of retired employees.

Adoption of new and/or amended IFRSs and IFRIC interpretations

- *IFRS 15 – Revenue from Contracts with Customers* The new standard introduces a comprehensive framework to determine whether, how much and when revenue should be recognised. The new standard replaces IAS 18, *Income*, IAS 11, *Construction contracts and their interpretations*. The Group initially applied IFRS 15 on 1 January 2018 retrospectively in accordance with the requirements of IAS 8, without using any practical exemptions. The adoption of IFRS 15 has not affected the timing or amount of recognition of the Group's commission income from contracts with customers.

The following are standards and interpretations that could have a significant impact on the Group:

- *IFRS 16 Leases (replaces IAS 17, IFRIC 4, SIC-15, SIC-27)*. Effective for reporting periods beginning on or after 1 January 2019. Earlier application is permitted if the entity also applies IFRS 15. The new standard establishes principles for the recognition, measurement, presentation and disclosure of leases in a way that is different to the currently applied accounting treatment. For qualifying lease assets, upon lease commencement, a lessee has to recognise a right-of-use asset and a lease liability. The right-of-use asset is initially measured at the amount of the lease liability plus any initial direct costs. Subsequently the right-of-use asset is measured using a cost model, unless specific other conditions persists. A right-of-use asset is measured at cost less any accumulated depreciation and impairment. The lease liability is initially measured as a discounted value of payments agreed over the lease term. A discount rate which discounts future payments to estimated present value is applied. For lessors classification of lease as an operating lease or a finance lease remains; therefore, the Group as a lessor estimates no significant direct effect from the new standard if it was implemented at the end of this reporting period.

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

For the Group as a lessee the major class of current operating lease contracts which qualify for right-of-use asset are rent agreements for the branch network and certain other premises used for Group operating needs. The majority of these agreements can be terminated early, but some of these agreements can be extended after expiry.

Most of the contracts can be terminated by the Group before their expiry date, but this is largely not accounted for in the estimates as there is no such intention at present. Nor does the lessor's right to terminate the contract before the maturity date is taken into account, although the Group has no power to exercise that right. Such a decision is based on the consideration that it is unlikely that the lessors will terminate a significant part of the contracts before their expiry date, since all contracts are concluded on terms that are in conformity with free market principles. Consequently, it is estimated for IFRS 16 purposes that the Bank has committed to lease the head office and other premises for another three years which is consistent with the planning period for internal property and equipment.

As of 1 January 2019, the Bank classified the asset and liability from the lease contracts at EUR 775 thousand.

The new standards, additions and interpretations that may not have a material impact on the Group are described below:

IFRS 17 - "Insurance contracts"

Amendments to IFRS 4 "Insurance Contracts" – Applying IFRS 9 "Financial statements" with IFRS 4 "Insurance contracts"

Annual improvements to IFRS

IAS 28 "Investments in Associates and Joint Ventures"

Plan Amendment, Curtailment or Settlement (Amendments to IAS 19)

IFRIC 23 "Uncertainty over Income Tax Treatments"

The Group and the Bank believe that the adoption of the new standards and interpretations will have no material impact on the financial statements at the time of their initial adoption, except for IFRS 16 as described above.

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

4 RISK MANAGEMENT

The Board of the Group and the Bank has developed a system for the identification, supervision and management of the key financial risks. The Bank's Council has approved this risk management system. This system is being constantly updated to take into account market conditions and the development of the Bank's and the Group's main operations. The following policies have been approved in order to achieve the Bank's and the Group's objectives related to capital adequacy, credit risk, operational risk management and anti-money laundering and terrorism financing:

1. Liquidity risk management policy;
2. Credit policy;
3. Credit risk management policy and strategy;
4. Risk transactions and risk control policy for large transactions;
5. Currency risk management policy;
6. Country risk management policy;
7. Interest rate risk management policy;
8. Policy on the prevention of laundering of proceeds derived from criminal activity and terrorism financing;
9. Operational compliance risk management policy;
10. Capital and liquidity adequacy assessment policy;
11. Operational risk management policy.
12. Reputation risk management policy.

The Board of the Bank is responsible for the implementation of the risk management policy approved by the Council of the Bank.

Comprehensive management of the risk control functions at the Bank is ensured by Chief Risk Officer (CRO). The CRO ensures that the following functions are performed:

- Set-up, supervision and timely improvement of the Bank's risk management system;
- Providing, on a regular basis, to the Bank's Council, Board and heads of relevant units comprehensive and clear information on the Bank's overall risk profile, all key risks to the Bank and compliance with the risk strategy;
- Advising and supporting the Bank's Council and Board in the development of strategies (including for risk) and in making other decisions related to the Bank's risks.

To promote independence, the CRO's duties exclude such functions that are connected with the performance of the activities to be controlled.

Liquidity risk

Liquidity risk is defined as the risk that the Group and the Bank may be unable to sustain its current and future cash flows and secure borrowings to prevent threats to the Bank's daily operations or overall financial position of the Bank (liquidity risk of financing) and risk that the Group and the Bank may be unable to sell its financial assets in the desired term without material losses due to a market collapse or insufficient market depth (market liquidity risk).

The Group and Bank have maintained adequate amounts of liquid assets to ensure compliance with liquidity ratio required by the normative acts of the Republic of Latvia of 30% against the Group and the Bank's current liabilities as at 31 December 2018 and 31 December 2017. According to the requirement set by the Financial and Capital Market Commission, during 2018 the Bank was required to maintain an individual liquidity ratio of 50%. The Bank is in compliance with this restriction. The Bank's liquidity ratio as at 31 December 2018 is 74.3% and that as at 31 December 2017 was 80.41%.

Regulations (EC) No.575/2013 introduced the concept of liquidity coverage ratio (LCR) and net stable funding ratio (NSFR) as measurements of the Bank's and the Group's liquidity position. Since 1 October 2016, LCR is calculated according to the Commission Delegated Regulation (EU) 2015/61. The minimum liquidity coverage ratio requirement is being introduced gradually. The minimum requirements to be complied with in the years 2016, 2017 and 2018 are accordingly as follows: 70%, 80% and 100%. The European Union's regulations on NSFR have not yet been finalised.

	2018	2018	2017	2017
	Group	Bank	Group	Bank
Liquidity reserve	86 110	86 110	140 389	140 389
Net cash outflow	13 476	13 489	21 339	21 241
Liquidity coverage ratio	639	638	658	661

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

The Group and Bank have approved internal limits for liquidity net position of the term structures of assets and liabilities in all currencies, EUR and USD. Internal limits for liquidity are used for risk analysis and control of liquidity and desirable structure of financing sources. An early warning system was developed in order to help identify exposure of the Bank's and the Group's liquidity position and necessity to attract additional sources. On the basis of data from early notification indices the Group and the Bank identify adverse trends impacting liquidity and analyse these trends and assess whether any hedging measures are required for liquidity risk. The Bank's Treasury Division organises and manages the daily process of resource management in order to ensure solvency, liquidity and profitability of the Bank. The Risk Management Department of the Bank evaluates and plans the term structure of assets and liabilities on a regular basis and carries out control over liquidity risk management, incl. monitors compliance with the required liquidity norms and internal limits defined by the Group and the Bank. Liquidity stress testing is performed using 6 scenarios. Scenarios include both internal and external factors. Stress testing is performed to the following stress levels: internal and typical to the Bank unfavourable events, changes of general market conditions, banking crisis and general market crisis at the same time. The impact of various shock scenarios on the regulating liquidity ratio and the Bank's income is analysed. The Board of the Group and the Bank develops and the Council approves a Business Continuity Plan for liquidity crises that specifies: preventive measures for the reduction of the likelihood of liquidity crisis, methods of timely identification of liquidity crisis and risk assessment, measures that have to be taken immediately in order to overcome liquidity crisis. The plan is tested on a regular basis. For maturity analysis of assets and liabilities refer to Note 35.

Credit risk

Credit risk is the risk that a counterparty, or obligor, fails to meet contractual obligations to the Group and the Bank.

The main objective of the Group's and the Bank's credit risk management is to ensure an optimal level of profit, financial stability of the Group and the Bank by adhering to the limits of tolerable credit risk across various categories, ensuring effective credit risk identification, measurement, monitoring and evaluation system, risk forecasting, identifying, developing and implementing risk mitigation measures.

The Group and the Bank have developed appropriate credit risk management policies, policies and procedures to manage the credit risk. The Credit Policy of the Group and the Bank sets out the basic principles for the management of credit exposures, credit risk diversification instruments, various permitted concentration levels and limits, basic principles for assessing the creditworthiness of borrowers and the document governing the decision on granting loans and changing credit conditions. The Group's and the Bank's credit risk management policies and strategies set out basic methods for credit risk management, identification, measurement and monitoring (ongoing supervision), control and mitigation, credit monitoring policies and quality evaluation criteria. The credit risk measurement system includes:

- risk assessment to make a decision on granting a loan;
- monitoring and management of credit risk;
- profit adjustment representing risk;
- risk analysis of credit portfolios;
- capital adequacy and capital distribution assessment;
- regular stress testing credit risk by the use of different scenarios.

The Group and the Bank apply various credit risk minimisation methods:

- limits and other restrictions, including limits on the total amount of loans granted to a single borrower or group of related persons, compliance with which is regularly monitored;
- credit risk diversification instruments;
- diversification of the loan portfolio;
- assessing the creditworthiness of borrowers and guarantors;
- collateral collateral and regular revaluation;
- establishment of special and / or additional credit conditions;
- credit monitoring and supervision, including through the Early Warning Indicator System;
- regular credit quality assessment, etc.

The Group and the Bank's Credit Policy and Credit Risk Management Policy and Strategy is reviewed and approved by the Board and Council. The Credit Committee and the Asset Measurement Committee have been established and are rigorously monitoring the Group and the Bank's credit risk.

Credit risk control at the Group and the Bank is carried out by a dedicated unit – Credit Risk Management Department. The Group and the Bank continuously monitor the performance of individual credit exposures and regularly reassesses

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

the creditworthiness of its customers. The review is based on the customer's most recent financial statements and other information submitted by the borrower, or otherwise obtained by the Bank. The current market value of collateral is regularly determined by either independent appraisal companies or the Bank's specialists, and in the event of negative movements in market prices the borrower is usually requested to put up additional security.

The Group and the Bank's maximum exposure to financial position credit risk is generally reflected in the carrying amounts of financial assets on the statement of financial position. The impact of possible netting of assets and liabilities to reduce potential credit exposure is not significant.

The Group and the Bank determine concentration limits and monitor credit risk concentration by industry/sector, geographic location, type of loan, country of residence, loan currency and type of collateral. Overall, concentration of the loan portfolio is verified across seven positions. For the analysis of concentration of credit risk in respect of loans and advances to customers refer to Note 11 "Loans" and Note 37 "Maximum credit risk". In order to meet the requirements defined in the policy of risk transactions and large risk transactions, the Group and the Bank perform an assessment and control of risks associated with all assets and liabilities, including contingent liabilities of the Group and the Bank on a regular basis. Limits are regarded as the main tool for the control of risk transactions.

Capital management

Regulation No 575/2013 requires credit institutions to maintain Common Equity Tier 1 capital ratio of 4.5%, Tier 1 capital ratio of 6% and total capital ratio of 8%. Capital ratios are calculated by the Bank as follows: Common Equity Tier 1 capital ratio is Tier 1 equity of the Bank expressed as a percentage against total exposures; Tier 1 capital ratio is Tier 1 capital expressed as a percentage against total exposures; and total capital ratio is equity expressed as a percentage against total exposures. Total exposures are the sum of notional risk weighted assets and contingent liabilities are determined as the sum of capital requirements of risks multiplied by 12.5. According to the requirement set by the Financial and Capital Market Commission, during 2017 the Bank was required to maintain an individual capital adequacy ratio of 10.2%, but starting from 15 March 2018 – 13.5%. In addition, according to the Credit Institutions Law the Bank is required to maintain a sufficient level of tier 1 capital to cover the total capital buffer requirement which consists of a capital buffer of 2.5% of total exposures and the specific countercyclical capital buffer determined as the total value of exposures multiplied by the countercyclical capital buffer rate specific for the particular credit institution. This requires that the individual capital adequacy ratio of the Bank be maintained at 10.2% which is increased by the total capital buffer requirement of 2.5% calculated as the sum of the capital buffer and the countercyclical capital buffer specific for the particular credit institution.

Assets have been weighted in accordance with pre-defined risk grades, determining risks in accordance with the amount of capital, necessary to maintain these assets. Off-balance sheet loan liabilities are weighted in accordance with lending risk adjustment grades and risk grades defined for liabilities of partners. The following risk grades are applied: 0%, 20%, 35%, 50%, 100%, 150%.

Capital management is carried out at the Bank according to the Capital and Liquidity Adequacy Assessment Policy. The process of capital adequacy assessment is organised at the Bank by CRO and implemented by the Risk Management Department.

An integral part of the capital adequacy assessment process at the Bank is the calculation, planning and maintenance of capital adequacy. The Bank's objectives when managing capital, which complies with the term "equity" in the statement of financial position, are:

- To comply with the capital regulatory requirements.
- To safeguard the Bank's ability to continue as a going concern so that it can continue to provide returns for shareholders.
- To maintain the strong capital base to support the development of its business.

Capital adequacy and the use of regulatory capital are monitored by the Bank's management on a regular basis, employing techniques based on the guidelines developed by the Basel Committee and the European Union directives, as implemented by the Financial and Capital Market Commission.

For the calculation of capital adequacy refer to Note 36 and for the impact on the ability of the Group and the Bank to continue as a going concern to Note 40.

Capital adequacy calculation of the Group and the Bank in accordance with the FCMC regulations implies several transitional adjustments as implemented by the EU and FCMC. Some of the transitional adjustments are expected to have a favourable impact for a number of future years which will then gradually reduce over time. The transitional adjustments are applicable to 2018 and later periods. For the purpose of capital adequacy calculation the Group and the Bank use the 5 year transition period provided under Regulation (EU) 2017/2395 (of 12 December 2017) concerning the impact of IFRS 9 on equity (CET1). Had IFRS 9 been implemented as at 31 December 2017 and had the transitional adjustments not been applied, the Bank's capital adequacy ratio would have reduced by 1.4 basis points and that of the Group by 1.3

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

basis points. In planning their future operations, the Group and the Bank take account of the implementation impact of IFRS 9 and foresee measures to be taken to reduce the negative impact as described in Note 40. The Group's and the Bank's long-term capital position for regulatory purposes is planned and managed in line with expected regulatory requirements.

Currency risk

Currency risk represents the potential losses from revaluation of balance sheet and off-balance-sheet items denominated in foreign currencies due to movements in foreign exchange rates. Gold is regarded as foreign currency. The objective of currency risk management is to mitigate the impact of adverse changes in exchange rates by minimising open positions in foreign currencies. The Bank does not use foreign currency open positions to generate income from speculative operations. During 2018, the Group and the Bank performed daily controls of compliance with limits defined in Currency risk management policy, for transactions with foreign currency. The Group and the Bank are subject to the Credit Institutions Law which requires that the open position in an individual currency should not exceed 10% of the Bank's capital and the total open foreign currency position should not exceed 20% of the Bank's capital applicable to limiting large exposures according to Regulation No 575/2013. In accordance with the Currency Risk Management Policy, structural units of the Group and Bank are cooperating with the Risk Management Department in evaluation of the currency risk component of the planned transactions and elaboration of hedging method for it. For currency analysis refer to Note 342

Interest rate risk

Interest risk is represented by possible negative influence on the Group and the Bank's income that can result from possible changes of interest rates. The GAP analysis is used for measurement of interest rates risk. Assets, liabilities, guarantees and contingent liabilities, subjected to interest rate risk, are divided in accordance with minimum period, left till possible repricing dates of interest rates. Basis risk is the likelihood to incur losses due to changes in interest rates on financial instruments with equal repricing dates but different base rates. Basis risk is managed by repricing loans (at floating interest rates) and deposits (with floating interest rates) to the same base rates. Repricing risk is the likelihood to incur losses due to changes in interest rates and different remaining maturities of assets, liabilities and contingent items. Yield curve risk is the likelihood to incur losses due to unexpected changes in the slope and shape of the yield curve. Repricing risk and yield curve risk are managed by matching interest rate sensitive assets and liabilities in each term interval (i.e. maintaining the net position of interest rate risk in each term interval within internal limits). Optionality risk is the likelihood to incur losses when the financial instrument directly (options) or indirectly (loans with early repayment option, demand deposits etc.) provides the customer with an option. Optionality risk is managed by setting sufficient commission fees for early withdrawal of a deposit and early repayment of a loan. The Group and Bank calculate the influence on yearly net interest income, with parallel increase of interest rates for 100 base points. In order to assess the impact of adverse changes in interest rates on profitability and economic value in market emergencies the Bank performs interest rate risk stress testing. In accordance with requirements of Interest rate risk management policy, interest rate risk has to be assessed whenever limits for financial instruments are determined. For the results of sensitivity analysis refer to Note 32.

Country risk

Country risk is represented by possible losses in cases, where a debtor of the Group and Bank, being non-resident, will not be able to meet its liabilities against the Group and Bank, due to political, social or economic circumstances of the country of residency of the debtor. Country risk is managed by the Board of the Bank. Based on analyses of economic, political and social conditions of each particular country, limits are determined for geographic concentration of assets, liabilities and off-balance sheet items, for the purpose of management of country risk. The evaluation provided by international rating agencies is considered when assessing country risk. Limitations have been approved for placement of assets in countries graded as non-OECD, as well as for limitations on residual balances of nostro accounts. Limits for partners and transaction types are determined based on evaluation of risks of country and partners. Compliance with the limits is ensured by the Risk Management Department via regular control. For geographical concentration refer to Note 31.

Anti money laundering and counter terrorism financing

The Bank's objective in managing the money laundering and terrorism financing (hereinafter – ML/TF) risk is to safeguard its reputation and stability in relationships with its customers and the society in general, cooperate with and provide services to trustworthy customers and cooperation partners whose business is understandable to the Bank to avoid, to the extent possible, being involved in money laundering and terrorism financing and to prevent damages resulting from the loss of customers and trust.

The improvement of the ML/TF risk management process is among the priorities of the Bank's Strategic Development Plan and during the reporting period the Bank made robust measures to improve the ML/TF risk management system, by establishing an internal control system for the ML/TF risk management in line with the specific business activities of the

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Bank based on an assessment of the level of ML/TF risk characteristic for its customers, operational geographies, services and products, and delivery channels that impact the Bank's exposure to the ML/TF risk.

ML/TF risk is managed by means of a new approach to assessing ML/TF risk which stipulates controlling the maximum permitted risk indicators against those set in the ML/TF risk management strategy. The exposure to ML/TF risk is determined, measured and analysed by the Bank on a regular basis to prevent significant ML/TF risks from increasing.

As part of ML/TF risk management, the Bank assesses sufficiency of its resources to manage ML/TF risk, including the amount of capital required to cover operational risks of the Bank. It is consistently assessed and controlled by the Bank by the help of a comprehensive capital adequacy assessment which results in a capital adequacy report based on the analysis of the risk profile of the Bank (including its Lithuanian branch).

The ML/TF risk is managed by the Bank by observing:

- applicable regulations of the countries in which the Bank operates;
- the operational development strategy of the Bank with the ML/TF risk management considered a significant element of it;
- the ML/TF risk management strategy, which details the framework for the ML/TF risk management and the internal control system for AML/CTF, measures restricting and reducing the ML/TF risk and the permissible exposure to the ML/TF risk for each year;
- the AML/CTF policy which specifies measures for implementing the ML/TF risk management strategy, and the responsibilities and accountability of structural units and employees in managing the ML/CF risk;
- internal requirements of the Bank concerning AML/CTF.

Under the impact of the volatile regulatory environment in 2018 the Bank paid particular attention to the development of ML/TF risk management methods in a most efficient manner to achieve high ML/TF risk prevention standards in full compliance with legal requirements and by making timely improvements and investments both in human resources and technologies.

The Bank's priorities during the reporting period as concerns the ML/TF risk management were the following:

- improvement of the ML/TF risk management system in line with the new regulation and technical capabilities;
- The Bank improved ML/TF and sanction risk management and controls, including it acquired and implemented constantly updated ACCUITY data bases on sanctioned persons, companies, ships, regions, dual use goods, EDD to prevent servicing transaction of persons subject to sanctions;
- The Bank implemented a new multi-stage customer risk scoring system by FICO Tonbeller (SIRON) and adjusted its operating processes by introducing a multi-level customer acceptance system;
- The Bank implemented automated systems for monitoring of customer transactions developed by FICO Tonbeller (SIRON), integrated them with the Bank's systems and adjusted them to its operational processes and risk management;
- The Bank implemented an automated ACCUITY system for pre-execution control of transactions and integrated it with other banking systems;
- The Bank has made significant additions to the capacity of the organisational structure for ML/TF risk management. The qualifications of the employees are being evaluated according to the principles laid down in the ML/TF risk management procedure in order to establish the level of qualification and whether appropriate resources are in place to manage the ML/TF risk provided for in the Strategy. Active work is carried out by Control Committee, which is a collegial structure that assesses the key ML/TF risks and makes decisions to implement preventive measures. Employees of the Bank improved their knowledge in external trainings involving foreign experts, including ACAMS. Overall, in 2017 the Bank's employees attended 40 training courses on AML/CTF;
- The Bank has fully implemented the recommendations formulated by independent USA consulting firms to raise the efficiency of the internal control system for ML/TF risk management.

The Bank continued changing its business strategy and significantly reduced its reliance on services provided to non-resident customers gradually reduced the number of USD payments and the number and scope of transactions of high-risk non-resident customers.

Also, the Financial and Capital Market Commission carried out a review of the Bank in 2017 in the field of anti-money laundering and counter terrorism financing regarding the previous periods, and provided guidelines and suggestions for the improvement of the Bank's internal control system, which the Bank continued to realise and implement in 2019.

According to the administrative agreement concluded in 2018, the Bank undertook to ensure the following independent AML/CFT risk management internal control system reviews:

- 1) on the compliance of the risk classification of customer base;
- 2) on the compliance of information technologies used in the management of ML/TF risk;

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

3) on the compliance of the Bank's internal control system for AML/CTF.

The first two reviews from a company of certified auditors, Deloitte, were acquired in the middle of 2018, receiving an evaluation and additional recommendations for the improvement of the respective area. By the end of 2018, the Bank had implemented all suggestions and recommendations resulting from the independent review, improved the technical functions of AML/TF information technology facilities, and registered in detail the functionality of customers' risk-scoring system.

In February 2019, an overall independent assessment of the Bank's AML/CTF internal control system was conducted by the sworn auditors' commercial company Deloitte. In March 2019, the Bank received a satisfactory opinion from the sworn auditors' commercial company Deloitte, as well as separate recommendations that will be implemented during the year 2019.

In line with the administrative agreement, in 2018 the Bank actively continued to improve its internal control system according to the planned measures approved by the Bank regarding the improvement of internal control system in the area of AML/TF. The most significant part of the measures was carried out in the second half of 2018 by introducing amendments and additions to AML/TF regulations, and by improving the functionality, scenarios and reports of the automated system for customer transaction monitoring, thus making the Bank's internal control system for AML/TF more efficient and reducing risks. By the end of 2018, the Bank has performed compliance review of all customers subject to due diligence, and an audit by purposefully reducing the number of customers posing a heightened AML/CFT risk.

In the following period, the Bank plans to continue reducing its AML/CFT risk exposure by declining high risk customers by effectively monitoring transactions and preventing suspicious transactions.

In 2018 the Bank continued and in 2019 will actively work to improve its automation systems in the area of AML/CFT, as well as improve efficiency of automated scenarios for the identification of suspicious transactions.

Operational risk

Operational risk is the risk of losses resulting from inadequate or improper internal processes, human and systems error, or the impact of external events, including legal risk but excluding strategic and reputational risk. Aiming to set up a system for the management of operational risk that would reduce the frequency of risk occurrences and the amount of loss to a level acceptable to the Bank and to safeguard the Bank's assets and capital, the Council has approved an appropriate policy. In order to implement this policy, the Board has approved a procedure that specifies the methods for identification, assessment, regular monitoring, control and mitigation of operational risk. Operational risk is managed by the Bank employing the following approaches: reporting of operational risk events; maintaining a data base of operational risk; establishing and controlling operational risk indicators any changes in which may indicate an increased likelihood of risk; self-assessing operational risk; and stress testing using both internal data and information on external operational risk events. The Bank uses hedging to reduce risk. Operational risk is managed by Risk Management Department.

To support the Bank's business continuity and to decrease operational losses due to *force majeure* circumstances the Board drafts and the Council approves and improves the business continuity plan and the information system recovery plan.

Operational compliance risk

Operational compliance risk is the risk that the Bank or its subsidiary may incur losses or legal obligations, be subject to sanctions or suffer impairment of reputation as a result of a failure to comply or a breach of compliance laws, regulations and standards. Operational compliance risk is inherent in all operations of the Bank. Management of operational compliance risk involves control, due identification, documentation, assessment, classification and efficient prevention of this risk or decreasing it to a level that the Bank finds acceptable, and follow-up of the risk. The operational compliance control is directed at the existing Bank's operations and due planning and execution of measures to prevent or decrease operational compliance risk with regard to new products and services of the Bank or other lines of business. Management of operational compliance risk is effected according to a policy approved by the Board using the following measures and approaches: systemic compliance reviews of the Bank's structural units, policies, internal procedures, other normative and informative materials; assessment of innovations; identification of operational compliance risks caused by external conditions; analysis of the reports of the Bank's structural units; analysis of statistical and analytical performance data; expert sounding board; analysis of reports of internal and external auditors and regulator or other parties; maintenance of an operational compliance risk data base and control over due prevention of identified risks or decreasing such risks to an acceptable level. Operational compliance risk is managed by the Compliance Control Unit who reports to the management on a regular basis.

5 ESTIMATES AND JUDGMENTS

The preparation of financial statements in conformity with IFRS as adopted by the EU requires management to make judgments, estimates and assumption that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Although these estimates are based on management's best knowledge of current events and actions, the actual results ultimately may differ from those estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to the accounting estimates are recognised in the period, in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Key sources of estimation uncertainty:

Going concern

These consolidated and separate financial statements are prepared on a going concern basis. The application of the going concern basis requires management to make a number of considerations and exercise judgment. Refer to Note 40.

Impairment of financial assets at amortised cost

Information about estimates resulting from the application of accounting policies that have the greatest effect on the amounts presented in the consolidated and separate financial statements is disclosed in the following notes: Note 3, Financial Instruments: classification of financial assets, measurement of the business model assets, and the contractual terms of a financial asset, in accordance with the 'principal and interest payments only' principle. Note 3, impairment losses: criteria for determining a significant increase in the credit risk of a financial asset from initial recognition, Including Forward-Looking Information in the Estimation of expected credit loss and models used to calculate expected credit loss.

Fair value measurement of financial assets

Financial instruments measured at fair value are based on their market values. The fair value of financial instruments measured at amortized cost is the present value of estimated future cash flows discounted at the market rate of interest. The fair value of current financial assets and liabilities approximates their amortized cost.

Fair value of investment property

In assessing the fair value of investment property, management relies on external experts, independent property valuers who have appropriate and recognised professional qualifications and recent experience in valuing the same category of property in the same place. External evaluations use the income measurement method or the benchmarking method (or both). The income method is based on the discounted estimated future cash flows of the property. The comparative method is based on recent transactions in similar properties

Correction of prior period errors:

In 2018, the Bank identified several errors in presentation and classification of financial statement line items:

- errors related to periodisation of several expenses presented as part of administrative expenses;
- errors related to incorrect classification of several assets and liabilities.

In order to correct these errors, as well as present users of financial statements with complete and correct information about the financial position and financial results of the Group and the Bank, restatement of comparative information was performed in accordance with requirements of IAS 8.

Detailed information on corrections of errors is as follows:

- Penalty from FCMC was received in June 2018 before the signing of financial statements for 2017, however, it was not recorded as adjusting event and was recorded in 2018. Error corrected via including respective expenses in administrative expenses for 2017.
- Audit fees for audit of financial statements for 2017 were included into expenses of 2018, thus creating cut-off error. Adjustment made to correct periodization of expenses.
- The Group and the Bank has corrected errors in calculation of accruals for unused annual leave for 2017, which resulted in additional expenses recognised in 2017 financial statements.
- Classification errors were corrected for following items:
 - o Cash in transit related to encashment operations was reclassified from "Other financial assets" to "Cash and cash equivalents" as it meets the definition of cash.
 - o Amounts receivable from several financial institutions were reclassified from "Loans" to "Other financial assets" as these do not represent loans by substance.
 - o Accrued expenses were reclassified from "Provisions" to "Other financial liabilities" as these are of certain amount and timing, and do not meet the definition of provision.

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Quantitative impact on financial statements:

The Group, 2017

Adjustments made to the statement of comprehensive income:	Comments	2017 before restatement (EUR'000)	Restatement (EUR'000)	2017 restated (EUR'000)
Personnel expenses	Accruals for unused annual leave	152	173	325
Administrative expenses – professional services	Audit fees for 2017	1,207	59	1,266
Administrative expenses – other	FCCM penalty correction	1,286	456	1,742
Profit or loss before tax		5,675	688	6,363
Loss for the year		5,675	688	6,363

The Group, 2017

Adjustments made to the statement of financial position:	Comments	2017 before restatement (EUR'000)	Restatement (EUR'000)	2017 restated (EUR'000)
Cash and demand deposits with the Bank of Latvia	Cash in transit reclassified to “Cash”	103,546	3,767	107,313
	- Cash in transit reclassified to “Cash” - Receivables from financial institutions reclassified to “Other assets”	9,313	(3,767)	6,043
Other assets			497	
Loans	Receivables from financial institutions reclassified to “Other assets”	77,282	(497)	76,785
Provisions	Reclassified to “Other liabilities” - Reclassified from “Provisions”	171	(168)	3
Other liabilities	- Additional accrued liabilities recognised	4,748	168	5,604
Adjustments to retained earnings for the year		9,912	688	10,600

The Group, 2017

Adjustments made to the cash flow statement	Comments	2017 before restatement (EUR'000)	Restatement (EUR'000)	2017 restated (EUR'000)
Loss before tax	Additional expenses recognised for 2017	(5,675)	(688)	(6,363)
Change in loans	Receivables from financial institutions reclassified to “Other assets”	12,532	497	13,029
Increase in other assets	- Cash in transit reclassified to “Cash” - Receivables from financial institutions reclassified to “Other assets”	(5,418)	3,767	(2,148)
			(497)	
Decrease in other liabilities	Additional accrued liabilities recognised	(5,552)	688	(4,864)
Cash flows from operating activities		13,283	3,767	17,050
Increase in cash and cash equivalents		12,800	3,767	16,567
Cash and cash equivalents at the end of reporting period	Cash in transit reclassified from “Other assets” to “Cash”	126,150	3,767	129,917

The Bank, 2017

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Adjustments made to the other comprehensive income:	Comments	2017 before restatement (EUR'000)	Restatement (EUR'000)	2017 restated (EUR'000)
Personnel expenses	Accruals for unused annual leave	152	173	325
Administrative expenses – professional services	Audit fees for 2017	1,207	59	1,266
Administrative expenses – other	FCMC penalty correction	1,286	456	1,742
Loss before tax		7,212	688	7,900
Loss for the year		7,212	688	7,900

The Bank, 2017

Adjustments made to the statement of financial position:	Comments	2017 before restatement (EUR'000)	Restatement (EUR'000)	2017 restated (EUR'000)
Cash and demand deposits with the Bank of Latvia	Cash in transit reclassified to “Cash”	103,546	3,767	107,313
Other assets	- Cash in transit reclassified to “Cash” - Receivables from financial institutions reclassified to “Other assets”	9,313	(3,767) 497	6,043
Loans	Receivables from financial institutions reclassified to “Other assets”	93,995	(497)	93,498
Provisions	Reclassified to “Other liabilities”	168	(168)	-
Other liabilities	- Reclassified from “Provisions” - Additional accrued liabilities recognised	4,500	168 688	5,356
Adjustments to retained earnings for the year		10,517	688	11,205

The Bank, 2017

Adjustments made to the cash flow statement	Comments	2017 before restatement (EUR'000)	Restatement (EUR'000)	2017 restated (EUR'000)
Loss before tax	Additional expenses recognised for 2017	(7,212)	(688)	(7,900)
Change in loans	Receivables from financial institutions reclassified to “Other assets” - Cash in transit reclassified to “Cash”	11,952	497 3,767	12,449
Increase in other assets	- Receivables from financial institutions reclassified to “Other assets”	(5,185)	(497)	(1,915)
Decrease in other liabilities	Additional accrued liabilities recognised	(5,106)	688	(4,418)
Cash flows from operating activities		13,283	3,767	17,050
Increase in cash and cash equivalents		12,800	3,767	16,567
Cash and cash equivalents at the end of reporting period	Cash in transit reclassified from “Other assets” to “Cash”	126,150	3,767	129,917

The Group, 2016

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Adjustments made to the statement of financial position:	Comments	2016 before restatement (EUR'000)	Restatement (EUR'000)	2016 restated (EUR'000)
Cash and demand deposits with the Bank of Latvia	Cash in transit reclassified to "Cash"	71,626	2,844	74,470
Other assets	- Cash in transit reclassified to "Cash" - Receivables from financial institutions reclassified to "Other assets"	6,256	(2,844) 500	3,912
Loans	Receivables from financial institutions reclassified to "Other assets"	104,648	(500)	104,148
Provisions	Reclassified to "Other liabilities"	193	(193)	-
Other liabilities	- Reclassified from "Provisions"	10,277	193	10,470
Adjustments to retained earnings for the year		4,237	-	4,237

The Bank, 2016

Adjustments made to the statement of financial position:	Comments	2016 before restatement (EUR'000)	Restatement (EUR'000)	2016 restated (EUR'000)
Cash and demand deposits with the Bank of Latvia	Cash in transit reclassified to "Cash"	71,626	2,844	74,470
Other assets	- Cash in transit reclassified to "Cash" - Receivables from financial institutions reclassified to "Other assets"	4,129	(2,844) 500	1,785
Loans	Receivables from financial institutions reclassified to "Other assets"	122,927	(500)	122,427
Provisions	Reclassified to "Other liabilities"	191	(191)	-
Other liabilities	- Reclassified from "Provisions"	9,587	191	9,778
Adjustments to retained earnings for the year		4,237	-	3,305

6 CASH AND DUE FROM THE BANK OF LATVIA

EUR'000	2018	2018	2017	2017
	Group	Bank	Group (restated)	Bank (restated)
Cash	3,025	3,025	4,125	4,125
Cash in Lithuanian branch	3,514	3,514	3,767	3,767
Balance with the Bank of Latvia (including minimum reserve deposit)	80,020	80,020	99,421	99,421
Total	86,559	86,559	107,313	107,313

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Due from the Bank of Latvia represents the EUR nominated balance on the correspondent account with the Bank of Latvia.

According to the regulations of the European Central Bank, the Bank is required to maintain obligatory reserves with the Bank of Latvia equal to 1% of the closing monthly balances due of deposits with agreed maturity or period of notice up to 2 years and debt securities issued with initial maturity up to 2 years. For all other liabilities included in the reserve calculation the applicable rate is 0%.

The compulsory reserve is compared to the Bank's average monthly balance on the correspondent account with the Bank of Latvia. The Bank's average cash and correspondent balance should exceed the compulsory reserve requirement.

On 1 January 2014 the Republic of Latvia joined the euro-zone and the Latvian Lat was replaced by the euro, as a result as of 1 January 2014 the obligatory reserve rates are determined by the European Central Bank, previously these rates were determined by Bank of Latvia.

As at 31 December 2018 and 31 December 2017 the Bank was in compliance with the above requirements.

7 DEMAND DEPOSITS WITH CREDIT INSTITUTIONS

(a) Geographical segments

EUR'000	2018	2018	2017	2017
	Group	Bank	Group	Bank
Credit institutions of OECD countries	4,797	4,797	8,326	8,326
Latvian credit institutions	905	905	12,292	12,292
Credit institutions of non-OECD countries	1,365	1,365	811	811
	7,067	7,067	21,429	21,429

The Bank maintained relationship with 25 correspondent banks (2017: 25).

The Bank significantly reduced its claims against credit institutions as a result of decrease in client deposits.

(b) The main correspondent banks of the Group and the Bank:

	2018	2017
	EUR'000	EUR'000
AS Rietumu Banka, Latvia	-	10,311 (48.1%)
Raiffeisen Bank International AG, Austria	2,008 (28.4%)	5,842 (27.3%)
ABLV Bank, AS, Latvia	-	1,676 (7.8%)
Lietuvas Banka, Lithuania	252 (3.6%)	223 (1.0%)

(c) Credit rating structure (Standard&Poors)

When allocating financial resources to monetary financial institutions of the Republic of Latvia, external credit ratings assigned to financial institutions are assessed, and for financial institutions that have not been granted an individual rating, their rating takes into account the rating of the parent bank as well as the financial and performance assessment. After commencement of business relations, the Group /the Bank monitors monetary financial institutions and follows compliance of granted limits with credit risk assessment.

EUR'000	2018	2018	2017	2017
	Group	Bank	Group	Bank
-rated from AAA to A-	27	27	256	256
- rated from BBB+ to BBB-	2,024	2,024	5,842	5,842
- rated from BB+ to B-	133	133	274	274
- not rated	4,883	4,883	15,057	15,057
	7,067	7,067	21,429	21,429

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

8 FINANCIAL ASSETS AT AMORTISED COST

(a) Latvian government bonds with fixed income

	Term	2018 Group EUR'000	2018 Bank EUR'000	2017 Group EUR'000	2017 Bank EUR'000
Latvian government bonds with fixed income	2018	-	-	2,110	2,110
(S&P – A, Moody's – A3)	2021	1,629	1,629	3,298	3,298
		<u>1,629</u>	<u>1,629</u>	<u>5,408</u>	<u>5,408</u>

(b) Other states government bonds with fixed income

EUR'000	Term	2018 Group	2018 Bank	2017 Group	2017 Bank
USA government bonds with fixed income (S&P- AA+, Moody's – Aaa)	2018	-	-	302	302
Alfa Bank, Russian Federation (S&P – BB, Moody's – Ba2)	2018	-	-	530	530
Lithuanian government bonds with fixed income (S&P – A-, Moody's – Baa1)	2018	-	-	849	849
Lithuanian government bonds with fixed income (S&P – A-, Moody's – Baa1)	2018	-	-	29,108	29,108
Lithuanian government bonds with fixed income (S&P – A-, Moody's – Baa1)	2020	2,371	2,371	2,354	2,354
		<u>2,371</u>	<u>2,371</u>	<u>33,143</u>	<u>33,143</u>
Total investments at amortised cost		<u>4,000</u>	<u>4,000</u>	<u>38,551</u>	<u>38,551</u>

9 FINANCIAL ASSETS BY CATEGORY

	2018 Group EUR '000	2018 Bank EUR '000	2017 Koncerns EUR '000	2017 Banka EUR '000
Held-to-maturity investments	-	-	6,356	6,356
Available-for-sale financial assets	-	-	32,481	32,481
Financial assets at amortised cost	4,000	4,000	-	-
Financial assets at fair value through other comprehensive income	344	344	-	-
	<u>4,344</u>	<u>4,344</u>	<u>38,837</u>	<u>38,837</u>

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

10 LOANS AND TERM DEPOSITS DUE FROM CREDIT INSTITUTIONS

EUR'000	2018	2018	2017	2017
	Group	Bank	Group	Bank
Term deposits with credit institutions	400	400	1,175	1,175
Other balances due from credit institutions	-	-	709	709
Total loans and term deposits	400	400	1,884	1,884

As at 31 December 2018 the Group and the Bank had amounts due from credit institutions of EUR 400 thousand (2017: EUR 709 thousand) that secured collaterals for the guarantees issued by the Bank.

Geographical classification:

EUR'000	2018	2018	2017	2017
	Group	Bank	Group	Bank
Residents of OECD countries	-	-	709	709
Residents of Latvia	400	400	1,175	1,175
Total loans and term deposits	400	400	1,884	1,884

11 LOANS TO CUSTOMERS

(a) Loans by groups are comprised as follows:

EUR'000	2018	2018	2017	2017
	Group	Bank	Group (restated)	Bank (restated)
Individuals	11,552	10,309	14,402	12,893
Legal entities	76,695	97,254	84,312	104,679
Personnel of the Bank	283	283	434	434
Total loans, gross	88,530	107,846	99,148	118,006
Impairment allowance	(26,791)	(28,946)	(22,363)	(24,508)
Total loans, net	61,739	78,900	76,785	93,498

(b) Loans by type:

EUR'000	2018	2018	2017	2017
	Group	Bank	Group (restated)	Bank (restated)
Loans and advances to customers	85,796	94,321	91,323	99,375
Credit lines	2,442	13,233	7,716	18,522
Overdrafts	292	292	109	109
Loans, gross	88,530	107,846	99,148	118,006
Impairment allowance*	(26,791)	(28,946)	(22,363)	(24,508)
Total loans, net	61,739	78,900	76,785	93,498

* As at 31 December 2018 the Group and the Bank impairment allowance include also 2 350 thousand EUR provisions for reducing credit risk concentration in accordance with regulatory requirements.

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

(c) Loans issued by industry, gross:

Legal entities	2018		2018		2017		2017	
	Group		Bank		Group (restated)		Bank (restated)	
Real estate property	30,499	39%	30,499	31%	30,928	36%	30,928	29%
Construction	2,437	3%	2,437	2%	5,972	7%	5,972	6%
Electricity	14,848	19%	14,848	15%	15,971	19%	15,971	15%
Wholesale and retail	8,408	11%	8,408	8%	10,327	12%	10,327	10%
Industrial markets	6,829	8%	6,829	7%	8,729	10%	8,729	8%
Transport, warehousing and communications	587	1%	587	1%	1,807	2%	1,807	2%
Loans issued to financial intermediaries	-	-	27,626	28%	-	-	27,649	26%
Finance lease	7,067	9%	-	-	7,281	9%	-	-
Others	6,020	10%	6,020	8%	3,297	5%	3,793	4%
Total	76,695	100%	97,254	100%	84,312	100%	105,176	100%
Individuals and personnel of the Bank								
Consumer loans	208	2%	208	2%	242	2%	242	2%
Credit card commitments	338	2%	338	3%	347	2%	347	3%
Mortgage loans	5,183	48%	5,183	49%	7,158	48%	7,158	54%
Finance lease	1,244	10%	-	-	1,509	10%	-	-
Business loans	4,621	37%	4,621	44%	5,439	37%	5,439	40%
Others	241	1%	242	2%	141	1%	141	1%
Total	11,835	100%	10,592	100%	14,836	100%	13,327	100%

(d) Loans by geographical classification:

EUR'000	2018		2017	
	Group	Bank	Group (restated)	Bank (restated)
Residents of Latvia	86,021	105,337	94,516	113,374
Residents of OECD countries	1,609	1,609	2,735	2,735
Residents of non-OECD countries	900	900	1,897	1,897
Loans to non-banking customers, gross	88,530	107,846	99,148	118,006
Impairment allowance	(26,791)	(28,946)	(22,363)	(24,508)
Loans and receivables, net	61,739	78,900	76,785	93,498

(e) Movements in the impairment allowance:

EUR'000	2018		2017	
	Group	Bank	Group	Bank
Balance at the beginning of the year	22,363	24,508	17,210	17,210
Increase in provisions for impairment of loans due to initial implementation of IFRS 9	1,662	1,662	-	-
<i>Increase in impairment allowance</i>	1,489	1,499	5,848	7,993
<i>Provisions for reducing credit risk concentration</i>	2,350	2,350	1,790	1,790
<i>Recovery of prior period loan loss allowances</i>	(1,023)	(1,023)	(2,198)	(2,198)
Changes in impairment allowance	2,816	2,826	5,440	7,585
Release of impairment allowances recognised in previous periods	(50)	(50)	(287)	(287)
Balance at the end of the reporting period	26,791	28,946	22,363	24,508

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

(f) Loans and accrued interest allocation, depending on delay of payments:

Group

EUR'000	Loans not overdue	Overdue loans						
		Up to 30 days	30-60 days	61-90 days	91-180 days	181-360 days	More than 360 days	
Loans and advances to customers 31 December 2018								
Gross loans and advances to customers	88,530	48,888	4,522	341	5,028	131	2,118	27,502
Impairment allowance	(26,791)	(12,308)	(935)	(25)	-	(45)	(1,247)	(12,231)
As at 31 December 2017								
Gross loans and advances to customers	99,148	62,256	10,637	4,987	571	10,700	5,628	4,369
Impairment allowance	(22,363)	(12,046)	(2,429)	(1,176)	(149)	(2,926)	(992)	(2,645)

Bank

EUR'000	Loans not overdue	Overdue loans						
		Up to 30 days	30-60 days	61-90 days	91-180 days	181-360 days	More than 360 days	
Loans and advances to customers 31 December 2018								
Gross loans and advances to customers	107,846	70,071	4,522	341	5,028	131	2,118	27,502
Impairment allowance	(28,946)	(14,465)	(935)	(24)	-	(45)	(1,247)	(12,230)
As at 31 December 2017								
Gross loans and advances to customers	118,006	84,456	8,650	4,749	205	10,066	5,628	4,252
Impairment allowance	(24,508)	(14,191)	(2,429)	(1,176)	(149)	(2,926)	(992)	(2,645)

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

The amounts shown in the table represent the gross carrying amount of the loans by type of collateral and do not necessarily represent the fair value of the underlying collateral:

	31 December 2018				As at 31 December 2017			
	Group EUR'000	%	Bank EUR'000	%	Group EUR'000	%	Bank EUR'000	%
Commercial buildings	48,438	54%	48,438	44%	53,805	54%	53,805	46%
Commercial assets pledge	7,177	8%	7,177	7%	9,489	10%	9,489	8%
Land mortgage	5,520	6%	5,520	5%	3,670	4%	3,670	3%
Mortgage on residential properties	15,350	17%	15,350	14%	20,422	20%	20,422	17%
Guarantee	1,442	1%	1,442	1%	1,369	1%	1,369	1%
Lease and other	8,995	10%	684	1%	8,985	9%	195	-
No collateral	1,608	4%	29,235	28%	1,408	2%	29,056	25%
Total	88,530	100%	107,846	100%	99,148	100%	118,006	100%

Significant credit risk concentration

As at 31 December 2018 and 2017, the Bank had 21 and 22 borrowers or groups of related borrowers, respectively, whose total loan liabilities exceeded 10% of the share capital of the Bank indicated in Note 36. The gross amount of the above loans as at 31 December 2018 and 31 December 2017 was EUR 57,944 thousand and EUR 67,834 thousand, respectively. An impairment allowance was recognised for the above loans as at 31 December 2018 and 31 December 2017 in the amount of EUR 20,455 thousand and EUR 16,931 thousand, respectively.

According to regulatory requirements, the Bank is not allowed to have a credit exposure to one client or a group of related clients of more than 25% of the Bank's equity. The Bank was in excess of these requirements as at 31 December 2018 in four instances (25.05% till 46.06%) and as at 31 December 2017 in nine instances (26.26% to 46.47%). In order to reduce the credit risk concentration, provisions for individual exposures have been created in the amount of 2,350 thousand EUR. However, there is a risk that non-compliance with the regulator's requirements may result in corrective measures or fines. The risk will be eliminated by increasing capital and reducing the amount of risk exposures.

(g) Breakdown of the Group's/ the Company's loans by their qualitative assessment after the adoption of IFRS 9:

	31 December 2018		1 January 2018	
	Group EUR'000	Bank EUR'000	Group EUR'000	Bank EUR'000
Credit risk has not increased significantly (Stage 1)	16,446	14,625	34,357	28,745
Credit risk has increased significantly (Stage 2)	14,584	25,224	4,419	18,540
Loans which have evidence of impairment (Stage 3)	57,499	67,996	60,867	71,218
Total gross loans	88,529	107,845	99,644	118,503
Impairment allowances	(25,558)	(27,713)	(24,029)	(26,175)
Total net loans	61,740	78,900	75,615	92,328
Expected loss allowances for balance sheet claims as at 01.01.2018.			(1,667)	(1,667)
			31 December 2017	
Total gross loans			99,644	118,503
Impairment allowances			(22,362)	(24,508)
Total net loans			77,282	93,995

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Group	Credit loss allowances				Gross carrying amount			
	Stage 1 (12- months ECL)	Stage 2 (lifetime ECL for SICR)	Stage 3 (lifetime ECL for credit- impaired)	Total	Stage 1 (12- months ECL)	Stage 2 (lifetime ECL for SICR)	Stage 3 (lifetime ECL for credit- impaired)	Total
As at 1 January 2018	1,251	416	22,362	24,029	34,357	4,419	60,867	99,644
Movements with impact on credit loss allowance charge for the period:								
Transfers:								
to lifetime (from Stage 1 to Stage 2)	(419)	234	-	(185)	(11,834)	10,857	-	(977)
to credit-impaired (from Stage 1 and Stage 2 to Stage 3)	(57)	(2)	280	221	(1,237)	(222)	1,239	(221)
from credit-impaired to lifetime (from Stage 3 to Stage 2)	-	21	-	21	-	484	(572)	(88)
to 12-months ECL (from Stage 2 to Stage 1)								
New originated or purchased	-	93	-	93	219	529	-	748
De-recognised during the period	(154)	(114)	(4)	(272)	(3,926)	(1,269)	(1,129)	(6,324)
Total movements with impact on credit loss allowance charge for the period:	(630)	232	276	(122)	(16,778)	10,379	(463)	(6,862)
Movements without impact on credit loss allowance charge for the period:								
Write-offs	-	-	(51)	(51)	-	-	(52)	(52)
Modification of contractual cash flows (no movements between stages)*	155	38	2,183	2,375	(1,134)	(214)	(2,513)	(3,861)
Other movements (changes in allowances for purposes of compliance)	-	-	560	560	-	-	(340)	(340)
Total movements without impact on credit loss allowance charge for the period	155	38	2,692	2,885	(1,134)	(214)	(2,905)	(4,252)
As at 31 December 2018	776	686	25,330	26,792	16,446	14,584	57,499	88,529

* Ordinary contractual cash flows from repayment of principal.

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Bank	Credit loss allowances				Gross carrying amount			
	Stage1 (12- months ECL)	Stage 2 (lifetime ECL for SICR)	Stage3 (lifetim e ECL for credit- impair ed)	Total	Stage1 (12- months ECL)	Stage 2 (lifetime ECL for SICR)	Stage3 (lifetime ECL for credit- impaired)	Total
As at 1 January 2018	1,251	416	24,508	26,175	28,745	18,540	71,218	118,503
Movements with impact on credit loss allowance charge for the period:								
Transfers:								
to lifetime (from Stage 1 to Stage 2)	(419)	234	-	(185)	(8,298)	7,357	-	(941)
to credit-impaired (from Stage 1 and Stage 2 to Stage 3)	(57)	(2)	280	221	(1,120)	(103)	1,076	(147)
from credit-impaired to lifetime (from Stage 3 to Stage 2)	-	21	-	21	-	322	(394)	(72)
New originated or purchased	-	93	-	93	1	1,199	-	1,200
De-recognised during the period	(154)	(114)	(4)	(272)	(3,754)	(1,328)	(1,011)	(6,093)
Total movements with impact on credit loss allowance charge for the period:	(630)	232	276	(122)	(13,172)	7,446	(328)	(6,053)
Movements without impact on credit loss allowance charge for the period:								
Write-offs	-	-	(51)	(51)	-	-	(52)	(52)
Modification of contractual cash flows (no movements between stages)*	155	38	2,192	2,385	(948)	(762)	(2,502)	(4,213)
Other movements (changes in allowances for purposes of compliance)	-	-	560	560	-	-	(340)	(340)
Total movements without impact on credit loss allowance charge for the period	155	38	2,702	2,894	(948)	(762)	(2,894)	(4,605)
As at 31 December 2018	776	686	27,486	28,947	14,625	25,224	67,996	107,845

* Ordinary contractual cash flows from repayment of principal.

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

(h) Finance lease receivables

Loans and advances to customers include the following finance lease receivables for leases of certain fixed assets where the Group is a lessor:

EUR'000	2018	2017
Gross investment in finance leases, receivable with maturity:		
Less than one year	3,448	3,289
Between one and five years	4,268	4,896
More than 5 years	1,142	1,368
Total gross investment in finance leases, receivables	8,858	9,553
Unearned interest income	(547)	(763)
Net investment in finance lease	8,311	8,790
 Net investments in finance leases with maturity:		
Less than one year	3,217	3,030
Between one and five years	4,039	4,506
More than 5 years	1,055	1,254
	8,311	8,790

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

12 PROPERTY AND EQUIPMENT

Group property and equipment

EUR'000	Buildings	Vehicles	Office equipment	Leasehold improvements	Total
Cost					
As at 31 December 2016	708	103	1,028	168	2,007
Additions	-	11	295	-	306
Sales	-	-	(25)	-	(25)
Disposals	-	-	(90)	(100)	(190)
As at 31 December 2017	708	114	1,208	68	2,098
Additions	-	-	147	2	149
Sales	-	-	4	(4)	-
Disposals	-	-	(238)	(57)	(295)
31 December 2018	708	114	1,121	9	1,952
Accumulated depreciation					
As at 31 December 2016	279	83	534	-	896
Depreciation for the reporting year	34	7	269	-	310
Depreciation of disposed fixed assets	-	-	(90)	-	(90)
As at 31 December 2017	313	90	713	-	1,116
Depreciation for the reporting year	35	7	268	-	310
Depreciation of disposed fixed assets	-	-	(238)	-	(238)
31 December 2018	348	97	743	-	1,188
Balance					
As at 31 December 2016	429	20	494	168	1,111
As at 31 December 2017	395	24	495	68	982
31 December 2018	360	17	378	9	764

Bank property and equipment

EUR'000	Buildings	Vehicles	Office equipment	Leasehold improvements	Total
Cost					
At 31 December 2016	708	20	1,028	168	1,924
Additions	-	2	295	-	297
Sales	-	-	(25)	-	(25)
Disposals	-	-	(90)	(100)	(190)
As at 31 December 2017	708	22	1,208	68	2,006
Additions	-	-	147	2	149
Reclassified	-	-	4	(4)	-
Disposals	-	-	(238)	(57)	(295)
31 December 2018	708	22	1,121	9	1,860
Accumulated depreciation					
At 31 December 2016	279	2	534	-	815
Depreciation for the reporting year	34	4	269	-	307
Depreciation of disposed fixed assets	-	-	(90)	-	(90)
As at 31 December 2017	313	6	713	-	1,032
Depreciation for the reporting year	35	5	268	-	308
Depreciation of disposed fixed assets	-	-	(238)	-	(238)
31 December 2018	348	11	743	-	1,102
Balance					
As at 31 December 2016	429	18	494	168	1,109
As at 31 December 2017	395	16	495	68	974
31 December 2018	360	11	378	9	758

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

13 INVESTMENT PROPERTY

The Group's investment property

	Land	Buildings	Total
Cost			
At 31 December 2016	4,181	12,705	16,886
Disposals	-	(2,175)	(2,175)
Acquired	2,166	-	2,166
As at 31 December 2017	6,347	10,530	16,877
Disposals	-	(501)	(501)
Acquired	-	551	551
Reclassified	-	435	435
31 December 2018	6,347	11,015	17,362
Change in fair value			
As at 31 December 2016	-	(976)	(976)
Revaluation impact	-	(705)	(705)
As at 31 December 2017	-	(1,681)	(1,681)
Revaluation impact	-	126	126
31 December 2018	-	(1,555)	(1,555)
Balance			
At 31 December 2016	4,181	11,729	15,910
As at 31 December 2017	6,347	8,849	15,196
31 December 2018	6,347	9,460	15,807

Income from lease of investment property in 2018 amounted to EUR 285 thousand (2017: EUR 332 thousand) and respectively maintenance expenses in 2018 amounted to EUR 140 thousand (2017: EUR 118 thousand).

Investment property consists of land, residential properties and commercial properties.

The fair value measurement for investment property has been categorised as Level 3 in the fair value hierarchy.

Group	2018	2017	Key assumptions
	Fair value EUR'000	Fair value EUR'000	
Residential real estate, Salaspils region	1,690	1,690	Determined based on comparable market transactions method and income method (50% and 50% respectively). Discount rate 9%.
Sand and gravel deposit, Talsi region	4,225	4,225	Discount rate of 15.12%. Cash flow period of 10 years Income based on sale of various quality of extracted sand and gravel.
Residential real estate, Riga	1,366	1,366	Land and building value determined based on comparable transactions. Price is EUR 2,651 per m ²
Commercial real estate, Daugavpils	628	628	Discount rate of 11.32%. Cash flow period of 6 years Occupancy rate of 80% to 95%. Rent ranging on average EUR 2,5 to EUR 10,38 per m ²

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

14 OTHER ASSETS

Other assets are as follows:

EUR'000	2018 Group	2018 Bank	2017 Group (restated)	2017 Bank (restated)
<i>Financial assets:</i>				
Funds in transit	-	-	3,050	3,050
Receivables	2,233	68	2,364	30
Credit card transactions in transit	331	331	598	598
Other financial assets	4,029	4,309	2,227	2,227
	6,593	4,708	8,239	5,905
<i>Non-financial assets:</i>				
Deferred expenses and accrued income	124	103	163	138
Other non-financial assets	-	-	1	-
	124	103	164	138
Total	6,717	4,811	8,403	6,043

15 DEPOSITS

EUR'000	2018 Group	2018 Bank	2017 Group	2017 Bank
Sector profile:				
Non-banking deposits				
Legal entities	58,859	58,863	126,864	126,865
Individuals	109,382	109,382	120,238	120,239
State institutions	313	313	2,320	2,320
Total non-banking deposits:	168,554	168,558	249,422	249,424
Total deposits	168,554	168,558	249,422	249,424

Geographical profile:

Residents	80,454	80,458	92,833	92,835
Non-residents	88,100	88,100	156,589	156,589
<i>Residents of OECD countries</i>	<i>20,856</i>	<i>20,856</i>	<i>59,545</i>	<i>59,545</i>
<i>Residents of non-OECD countries</i>	<i>67,244</i>	<i>67,244</i>	<i>97,044</i>	<i>97,044</i>
Total deposits	168,554	168,558	249,422	249,424

EUR'000	2018 Group	2018 Bank	2017 Group	2017 Bank
Demand deposits				
Legal entities	54,457	54,461	120,416	120,417
Private individuals	73,448	73,448	76,794	76,794
State institutions	313	313	2,320	2,320
Total demand deposits	128,218	128,222	199,530	199,531
Term deposits				
Legal entities	4,402	4,402	6,448	6,448
Private individuals	35,934	35,934	43,444	43,445
Total term deposits	40,336	40,336	49,892	49,893
Total current accounts and deposits from non-banking customers	168,554	168,558	249,422	249,424

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

As at 31 December 2018, the Bank maintained customer deposit balances of EUR 81 thousand (2017: EUR 531 thousand) which were blocked by the Bank as collateral for loans and other contingent liabilities granted by the Bank.

Concentrations of current accounts and customer deposits

As at 31 December 2018 and 31 December 2017 the Bank had no customers whose balances exceeded 10% of total customer deposits.

16 SUBORDINATED DEBT

Subordinated liabilities as at 31 December 2018 comprise loans received from 5 private individuals and 2 legal entities (31 December 2017: 8 private individuals and 1 legal entity).

	Maturity	Interest rate	31 December 2018		31 December 2017	
			EUR'000		EUR'000	
			Group	Bank	Group	Bank
Loan No. 5	26.04.2025	4%	427	427	427	427
Loan No. 7	25.11.2018	3.6%	-	-	1,300	1,300
Loan No. 8*	22.03.2019	3.6%	1,500	1,500	1,500	1,500
Loan No. 10	29.04.2018	2%	-	-	284	284
Loan No. 11	09.07.2018	4.25%	-	-	300	300
Loan No. 12	08.09.2018	3.75%	-	-	300	300
Loan No. 13	05.04.2023	4%	280	280	280	280
Loan No. 14	02.09.2022	4%	427	427	427	427
Loan No. 15	01.09.2022	4%	285	285	285	285
Loan No. 16	31.03.2022	3.5%	280	280	280	280
Loan No. 18	28.08.2023	3.75%	199	199	-	-
Total			3,398	3,398	5,383	5,383

*Loan Nr.8 has been fully paid on 22 March 2019.

Subordinated loans are to be satisfied after the claims of all other creditors of the Bank, but before claims of shareholders of the Bank in case of liquidation of the Bank.

17 OTHER LIABILITIES

Other liabilities are as follows:

EUR'000	2018		2017	
	Group	Bank	Group	Bank
<i>Financial liabilities</i>				
Funds in transit	933	933	2,161	2,161
Unmatched funds	42	42	90	90
Other financial liabilities, incl.	1,006	1,006	1,286	1,286
<i>Funds to secure loans</i>	737	737	1,017	1,017
	3,537	3,537	9,551	9,551
<i>Non-financial liabilities</i>				
Accrued expenses and deferred income	716	501	2,067	1,131
	716	501	2,067	1,131
Total	2,697	2,482	5,604	5,356

Cash in transit includes amounts requested by clients for payment with a value date of 2 January 2019 and 2018, respectively.

Unmatched funds include amounts for which the Bank has not matched incoming funds to its client accounts. Unmatched accounts are matched within ten working days after they are received.

Other liabilities include provisions for unused vacations in amount of EUR 287 thousand for the Group and the Bank (2017: EUR 350 thousand and EUR 324 thousand, respectively).

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

18 SHARE CAPITAL

	Nominal value (EUR)	31 December 2018		31 December 2017	
		Number of shares	Share capital, EUR'000	Number of shares	Share capital, EUR'000
Ordinary shares	71.10	233,451	16,598	233,451	16,598
Shareholders					
		2018		2017	
		Number of shares	%	Number of shares	%
Private individuals		193,531	82.90	210,339	90.10
Legal entities		39,920	17.10	23,112	9.90
Total		233,451	100	233,451	100

The Bank's capital is registered and fully paid. Ordinary shares rank equally with respect to dividends, as may be declared, and entitle all holders to equal voting rights at the shareholders' meeting. All shares rank equal with respect to residual assets. As at 31 December 2018, there were 7 shareholders – 2 legal entities and 5 private individuals (As at 31 December 2017: 6 – 1 legal and 5 individuals).

Upon privatization of the Bank in accordance with statutory requirements in force as at the date of privatization a reserve capital of EUR 149 thousand was created. In May 2014, the previous shareholder dispossessed the shares without any claim and transferred it to the Bank. In November 2014, the Bank sold these shares for EUR 4,006 thousand and starting from 31 December 2014, this investment is recognised as reserve capital.

The use of share premium is defined by applicable Latvian legislation.

19 INTEREST INCOME

EUR'000	2018	2018	2017	2017
	Group	Bank	Group	Bank
Interest income calculated using effective interest rate:				
Interest income on assets at amortised cost:	2,243	2,243	3,505	3,603
<i>Loans and receivables</i>	2,127	2,127	2,880	2,978
<i>Loans and receivables from banks</i>	116	116	404	404
<i>Held-to-maturity investments</i>	-	-	221	221
Interest income on assets at fair value	240	240	-	-
Available-for-sale securities	-	-	417	417
Interest income from finance lease	23	-	-	-
Total	2,506	2,483	3,922	4,020

20 INTEREST EXPENSE

EUR'000	2018	2018	2017	2017
	Group	Bank	Group	Bank
Interest expenses on liabilities at amortised cost:				
Current accounts and deposits of customers	1,542	1,542	1,587	1,587
Total	1,542	1,542	1,587	1,587

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

21 FEE AND COMMISSION INCOME

	2018	2018	2017	2017
EUR'000	Group	Bank	Group	Bank
Commissions from money transfers, cash operations and servicing accounts	7,580	7,580	4,365	4,365
Fees from cards services	2,010	2,010	1,903	1,903
Commissions from guarantees	56	56	82	82
Brokerage fees	97	97	122	122
Others	334	331	181	179
Total	10,077	10,074	6,653	6,651

22 FEE AND COMMISSION EXPENSE

	2018	2018	2017	2017
EUR'000	Group	Bank	Group	Bank
Commissions paid to correspondent banks	245	245	319	319
Commissions for transactions with payment cards	1,531	1,531	1,451	1,451
Fees for operations with securities	97	97	78	78
Others	390	390	218	218
Total	2,263	2,263	2,066	2,066

23 GAIN ON TRADING WITH FINANCIAL INSTRUMENTS, NET

	2018	2018	2017	2017
EUR'000	Group	Bank	Group	Bank
Profit from foreign currency transactions	2,521	2,879	2,531	2,531
Profit / (loss) from revaluation of foreign exchange	(315)	(317)	97	89
Profit/(loss) from transactions with financial instruments	(84)	(84)	24	24
Profit/(loss) from revaluation of investments	(2)	(2)	1	1
Total	2,116	2,476	2,653	2,645

24 ADMINISTRATIVE EXPENSES

Salaries, wages and related social security contributions represent the basic remuneration of the employees, social security contributions as well as other personnel expense. During the years ended 31 December 2018 and 2017, the Group and the Bank employed on average 181 and 228 employees, respectively. Administrative expenses are as follows:

	2018	2018	2017	2017
EUR'000	Group	Bank	Group (restated)	Bank (restated)
Salaries to members of the Council and the Board	329	329	415	415
Personnel salaries and wages	3,964	3,930	4,162	4,133
State compulsory social insurance contributions	1,019	1,011	1,025	1,019
Professional services	1,104	1,089	1,266	1,266
Rent of premises and other maintenance expenses	636	636	943	943
Depreciation of property and equipment and intangible assets	329	327	311	307
Office supplies	24	24	35	35
Advertising and marketing	23	23	31	31
Others	1,009	909	1,878	1,742
Total	8,437	8,278	10,066	9,891

The administrative expenses for 2017 include a provision of EUR 1,345 thousand for the fine imposed by the Financial and Capital Market Commission. The fine was paid in 2018.

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Total audit expenses are included in the professional services item:

	2018 Group	2018 Bank	2017 Group (restated)	2017 Bank (restated)
Annual and interim audit fees	145	145	87	87
Other audit fees and similar expenses	-	-	39	39

Total personnel expenses are included in the following profit or loss caption:

EUR'000	2018 Group	2018 Bank	2017 Group	2017 Bank
Administrative expenses	5,312	5,270	5,429	5,394
Total	5,312	5,270	5,429	5,394

Total depreciation of property and equipment and leasehold improvements is included in the following profit or loss caption:

EUR'000	2018 Group	2018 Bank	2017 Group	2017 Bank
Administrative expenses	329	327	311	307
Total	329	327	311	307

25 TAXES

Corporate Income Tax

EUR'000	2018 Group	2018 Bank	2017 Group	2017 Bank
Corporate Income Tax	1	1	-	-
Corporate Income Tax	1	1	-	-

In the reporting year

Current tax for the reporting year is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the reporting date, and any adjustment to tax payable in respect of previous years. See below for information on changes effective as of 1 January 2018.

Changes to the calculation of Corporate Income Tax as of 1 January 2018

As of 1 January 2018, the new Law on Enterprise Income Tax of the Republic of Latvia comes into effect setting out a conceptually new regime for paying taxes. As of the date, the tax rate will be 20% instead of the current 15%, the taxation period will be one month instead of a year and the taxable base will include:

- distributed profit (dividends calculated, payments equalled to dividends, conditional dividends) and
- conditionally or theoretically distributed profit (non-operating expenses, doubtful debts, excessive interest payments, loans to related parties, decrease of income or excessive expenses which are incurred by entering transactions at prices other than those on the market that should be calculated using the methodology determined by the Cabinet of Ministers, benefits bestowed by the non-resident upon its staff or board (council members) regardless of whether the receiving party is a resident or a non-resident, if they relate to the operation of a permanent establishment in Latvia, liquidation quota).

The use of tax losses carried forward from previous periods is limited: it will be possible to utilise these losses to decrease the amount of tax calculated on dividends in the reporting period by not more than 50%. It will be possible to carry forward unused tax losses and utilise them in the previously described manner only until 2022.

According to the new Law on Enterprise Income Tax of the Republic of Latvia adopted on 28 July 2017, and effective as of 1 January 2018, a 20% rate is only applied to distributed profit, while a 0% rate is expected to be applied to undistributed profits. Therefore, deferred tax assets and liabilities are recognisable as nil. This principle has been applied in the Bank's and Group's financial statements for the year ended 31 December 2018.

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

26 CASH AND CASH EQUIVALENTS

EUR'000	2018	2018	2017	2017
	Group	Bank	Group (restated)	Bank (restated)
Cash	3,025	3,025	4,125	4,125
Current placements with the Bank of Latvia	80,020	80,020	99,421	99,421
Demand deposits and term deposits with other credit institutions with initial maturity of less than three months	7,067	7,067	22,604	22,604
Cash in Lithuanian branch	3,513	3,513	3,767	3,767
Total	93,625	93,625	129,917	129,917

27 INVESTMENTS IN SUBSIDIARIES

Investments in subsidiaries

Name of subsidiary	Share %	
	2018	2017
MTB Finance AS*	100%	100%

EUR'000	31 December	31 December
	2018	2017
Investments in subsidiaries	44	44
Impairment allowance	(44)	(44)
Investment in subsidiary, net	-	-

AS "MTB Finance" owns 100% shares of MULT YATIRIM VE DANISMANLIK EMLAK TURIZM INSAAT ITHALAT IHRACAT SANAYI TICARET LIMITED SIRKETI (registration No. 52424) in Turkey, Antalya district, Kumluca region, Karaoz micro region, Jenica village.

EUR'000	Current assets	Long-term assets	Total Assets	Current liabilities	Non-current liabilities	Total liabilities	Net assets
31 December 2018	8,306	17,601	25,907	21,498	6,722	28,220	(2,313)
31 December 2017	5,358	20,997	26,355	21,227	6,868	28,095	(1,740)
	Income	Expenses	Net loss				
31 December 2018	734	(1,284)	(550)				
31 December 2017	1,410	(2,072)	(662)				

28 RELATED PARTY TRANSACTIONS

(a) Control relationships

Related parties are defined as shareholders of the Bank who have a significant holding in the Bank and spouses, parents and children of the shareholders who are natural persons, members of the Council and the Board, head of the Internal Audit Service, CRO, compliance controller and public controller, the spouses, parents and children of these persons, and companies in which they have a controlling interest. In line with Section 43 of the Credit Institution Law, risk transactions with related parties must not exceed 15% of the Bank's equity, applicable to limiting large exposures according to Regulation No 575/2013. As at 31 December 2018, the Bank did not observe this requirement and its risk transactions with related parties amounted to 22% (taking into account provision for credit risk reduction, refer to Note 11). During the reporting period, the Bank performed measures to prevent this violation, and as at the date of issue of these financial statements, the bank complies with the restriction.

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

The transactions carried out with AS MTB Finance (Latvia) in the year ended 31 December 2018 were as follows:

EUR'000	2018 Bank	Average weighted rate	2017 Bank	Average weighted rate
Loans issued to AS MTB Finance	27,626	1.56%	27,649	1.53%
Deposits from AS MTB Finance	4	-	2	-

The Bank's and the Group's assets and liabilities from transactions with related parties:

EUR'000	2018 Group	2018 Bank	2017 Group	2017 Bank
<u>Credit exposures to Other related parties, net</u>				
Loans to customers, net				
- Management	100	100	106	106
- Consolidated subsidiaries	-	25,471	-	25,503
- Entities related to the shareholders	1,564	1,564	3,985	3,985
Credit exposures to related parties, net	1,664	27,135	4,091	29,594
EUR'000	2018 Group	2018 Bank	2017 Group	2017 Bank
<u>Liabilities to Other related parties</u>				
Deposits				
- Management	89	89	730	730
- Consolidated subsidiaries	-	4	-	2
- Others	102	102	704	704
Liabilities to related parties	191	195	1,434	1,436

The Bank's and the Group's operating income and expenses from transactions with related parties:

EUR'000	2018 Group	2018 Bank	2017 Group	2017 Bank
<i>Interest income</i>				
- Management and companies related to the shareholders	163	163	18	18
- Consolidated subsidiaries	-	424	-	406
<i>Interest expenses</i>				
- Management	-	-	(9)	(9)

The total amount of related party loans and deposits at the year end:

EUR'000	2018 Bank	Average weighted rate	2017 Bank	Average weighted rate
Deposits from AS MTB Finance and other related parties	195	0.1%	1,434	1.11%
Loans to other related parties				
Opening balance	4,091		1,315	
Issued loans in current year	24		3,013	
Matured loans in current year	(2,451)		(237)	
Loans closing balance	1,664	2.32%	4,091	2.30%

Remuneration to the Council and the Board:

EUR'000	2018 Group	2018 Bank	2017 Group	2017 Bank
Remuneration to the Council and the Board	329	329	415	415
Total	329	329	415	415

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Transactions with related parties carried out in the year:

EUR'000	2018	2018	2017	2017
	Group	Bank	Group	Bank
Interest income	163	587	18	406
Interest expenses	-	-	(9)	(9)
Total	163	587	9	397

29 ASSETS AND LIABILITIES UNDER TRUST MANAGEMENT

Assets EUR'000	2018	2018	2017	2017
	Group	Bank	Group	Bank
Fiduciary loan	1,000	1,000	2,084	2,084
Total	1,000	1,000	2,084	2,084

Liabilities EUR'000	2018	2018	2017	2017
	Group	Bank	Group	Bank
Funds received from individuals	-	-	500	500
Funds received from corporate customers	1,000	1,000	1,584	1,584
Total	1,000	1,000	2,084	2,084

Liabilities under trust management consist of funds of non-resident clients in the total amount of EUR 1,000 thousand.

A fiduciary loan is a transaction whereby the Group and the Bank have attracted a fiduciary deposit that has been issued to a borrower specified by those depositors on behalf of the depositors and at the depositor's risk. The property owned by clients is kept under management separately from the property of the Group and the Bank and is kept in separate accounts at credit institutions through which the funds are invested. Assets under management often represent a securities portfolio separated from the Bank's and the Group's assets, which is treated as a joint management object with its own structure, liquidity degree, sources of resources, yield and common risk. The Group and Bank is engaged in securities purchase and sales on behalf of their clients. Such securities are not recognised on statement of financial position of the Group and the Bank.

30 CONTINGENT LIABILITIES

At any time the Bank has outstanding commitments to extend credit. These commitments take the form of approved loans, credit card limits and overdraft facilities.

The Bank provides financial guarantees and letters of credit to guarantee the performance of customers to third parties. These agreements have fixed limits and generally extend for a period of up to ten years. The Bank also provides guarantees by acting as settlement agent in securities borrowing and lending transactions

The contractual amounts of commitments are set out in the following table by category. The amounts reflected in the table for commitments assume that amounts are fully advanced. The amounts reflected in the table for guarantees and letters of credit represent the maximum exposure that would be recognised in the statement of comprehensive income if counterparties failed to honour their contracted liabilities to any extent.

EUR'000	2018	2018	2017	2017
	Group	Bank	Group	Bank
Loans and credit line liabilities	1,299	1,299	4,354	4,354
Guarantees and letters of credit	1,590	1,590	756	756
Total	2,889	2,889	5,110	5,110

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

31 GEOGRAPHICAL CONCENTRATION OF ASSETS, LIABILITIES, EQUITY AND CONTINGENT LIABILITIES

The geographical segmentation of the Bank's and the Group's assets, liabilities and contingent liabilities as at 31 December 2018 was as follows:

Group

	Latvia	OECD countries	CIS countries	Other countries	Total
31 December 2018					
Assets EUR'000					
Cash and balances due from the Bank of Latvia	82,805	-	-	3,754	86,559
Financial assets at amortised cost	1,629	-	-	2,371	4,000
Financial assets at fair value through other comprehensive income	2	342	-	-	344
Demand deposits with credit institutions	905	4,797	1,091	274	7,067
Loans and term deposits due from credit institutions	400	-	-	-	400
Loans and advances to customers	60,757	190	131	661	61,739
Intangible assets	9	-	-	-	9
Property and equipment	755	-	-	9	764
Investment properties	15,807	-	-	-	15,807
Other assets	2,702	4,001	1	13	6,717
Total assets	165,771	9,330	1,223	7,082	183,406
31 December 2018					
Liabilities EUR'000					
Deposits	80,454	20,856	12,762	54,482	168,554
Subordinated liabilities	1,500	427	991	480	3,398
Other liabilities	2,667	-	-	30	2,697
Provisions	53	-	-	-	53
Capital and reserves	8,704	-	-	-	8,704
Total equity, reserves and liabilities	93,378	21,283	13,753	54,992	183,406
Contingent liabilities and commitments	2,882	-	-	7	2,889

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

31 GEOGRAPHICAL CONCENTRATION OF ASSETS, LIABILITIES, EQUITY AND CONTINGENT LIABILITIES (CONTINUED)

Bank

	Latvia	OECD countries	CIS countries	Other countries	Total
31 December 2018					
Assets EUR'000					
Cash and balances due from the Bank of Latvia	82,805	-	-	3,754	86,559
Financial assets at amortised cost	1,629	-	-	2,371	4,000
Financial assets at fair value through other comprehensive income	2	342	-	-	344
Demand deposits with credit institutions	905	4,797	1,091	274	7,067
Loans and term deposits due from credit institutions	400	-	-	-	400
Loans and advances to customers	77,917	191	131	661	78,900
Intangible assets	9	-	-	-	9
Property and equipment	749	-	-	9	758
Other assets	796	4,001	1	13	4,811
Total assets	165,212	9,331	1,223	7,082	182,848
31 December 2018					
Liabilities EUR'000					
Deposits	80,458	20,856	12,762	54,482	168,558
Subordinated liabilities	1,500	427	991	480	3,398
Other liabilities	2,452	-	-	30	2,482
Provisions	53	-	-	-	53
Capital and reserves	8,357	-	-	-	8,357
Total equity, reserves and liabilities	92,820	21,283	13,753	54,992	182,848
Contingent liabilities and commitments	2,882	-	-	7	2,889

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

31 GEOGRAPHICAL CONCENTRATION OF ASSETS, LIABILITIES, EQUITY AND CONTINGENT LIABILITIES (CONTINUED)

The geographical segmentation of the Bank's and the Group's assets, liabilities and contingent liabilities as at 31 December 2017 was as follows:

Group

	Latvia	OECD countries	CIS countries	Other countries	Total
As at 31 December 2017					
Assets EUR'000					
Cash and balances due from the Bank of Latvia	102,715	-	-	4,598	107,313
Held-to-maturity investments	3,700	-	-	2,656	6,356
Available-for-sale financial assets	1,711	30,240	-	530	32,481
Demand deposits with credit institutions	12,292	8,326	588	223	21,429
Loans and term deposits due from credit institutions	1,175	709	-	-	1,884
Loans and advances to customers	73,873	1,015	884	1,013	76,785
Held-for-trading financial assets	28	-	-	-	28
Property and equipment	970	-	-	12	982
Investment property	15,068	128	-	-	15,196
Other assets	2,523	2,815	3,052	13	8,403
Total assets	214,055	43,233	4,524	9,045	270,857
As at 31 December 2017					
Liabilities EUR'000					
Deposits	92,833	59,545	22,571	74,473	249,422
Subordinated liabilities	-	-	3,883	1,500	5,383
Other liabilities	5,575	-	-	29	5,604
Capital and reserves	10,448	-	-	-	10,448
Total equity, reserves and liabilities	108,856	59,545	26,454	76,002	270,857
Contingent liabilities and commitments	5,104	-	-	6	5,110

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

31 GEOGRAPHICAL CONCENTRATION OF ASSETS, LIABILITIES, EQUITY AND CONTINGENT LIABILITIES (CONTINUED)

Bank

	Latvia	OECD countries	CIS countries	Other countries	Total
As at 31 December 2017					
Assets EUR'000					
Cash and balances due from the Bank of Latvia	102,715	-	-	4,598	107,313
Held-to-maturity investments	3,700	-	-	2,656	6,356
Available-for-sale financial assets	1,711	30,240	-	530	32,481
Demand deposits with credit institutions	12,292	8,326	588	223	21,429
Loans and term deposits due from credit institutions	1,175	709	-	-	1,884
Loans and advances to customers	90,587	1,014	884	1,013	93,498
Held-for-trading financial assets	28	-	-	-	28
Property and equipment	962	-	-	12	974
Other assets	766	2,212	3,052	13	6,043
Total assets	213,936	42,501	4,524	9,045	270,006
As at 31 December 2017					
Liabilities EUR'000					
Deposits	92,835	59,545	22,571	74,473	249,424
Subordinated liabilities	-	-	3,883	1,500	5,383
Other liabilities	5,307	-	-	29	5,336
Capital and reserves	9,863	-	-	-	9,863
Total equity, reserves and liabilities	108,005	59,545	26,454	76,002	270,006
Contingent liabilities and commitments	5,104	-	-	6	5,110

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

32 INTEREST RATE REPRICING ANALYSIS

The interest rate repricing analysis of the Bank's and the Group's assets and liabilities as at 31 December 2018 was as follows:

Group

	Less than 1 month	1 – 3 months	3 – 6 months	6 – 12 months	1 – 5 years	Over 5 years	Not sensitive to changes in interest rates	Total
EUR'000								
Assets								
Cash and balances due from the Bank of Latvia	80,020	-	-	-	-	-	6,539	86,559
Demand deposits with credit institutions	7,067	-	-	-	-	-	-	7,067
Financial assets at amortised cost	-	-	-	-	4,000	-	-	4,000
Financial assets at fair value through other comprehensive income	-	-	-	-	-	-	344	344
Loans and advances to customers	23,393	1,852	13,966	9,601	10,929	1,998	-	61,739
Loans and term deposits due from credit institutions	-	400	-	-	-	-	-	400
Intangible assets	-	-	-	-	-	-	9	9
Property and equipment	-	-	-	-	-	-	764	764
Investment property	-	-	-	-	-	-	15,807	15,807
Other assets	-	-	-	-	-	-	6,717	6,717
Total financial assets	110,480	2,252	13,966	9,601	14,929	1,998	30,180	183,406
Liabilities								
Deposits	134,714	4,842	6,895	12,074	10,029	-	-	168,554
Subordinated liabilities	-	1,500	-	-	1,471	427	-	3,398
Other liabilities	-	-	-	-	-	-	2,750	2,750
Total liabilities	134,714	6,342	6,895	12,074	11,500	427	2,750	174,702
Capital and reserves	-	-	-	-	-	-	8,704	8,704
Total liabilities, capital and reserves	134,714	6,342	6,895	12,074	11,500	427	11,454	183,406
Interest rate risk	(24,234)	(4,090)	7,071	(2,473)	3,429	1,571	18,759	-

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

32 INTEREST RATE REPRICING ANALYSIS (CONTINUED)

Bank

	Less than 1 month	1 – 3 months	3 – 6 months	6 – 12 months	1 – 5 years	Over 5 years	Not sensitive to changes in interest rates	Total
EUR'000								
Financial assets								
Cash and balances due from the Bank of Latvia	80,020	-	-	-	-	-	6,539	86,559
Demand deposits with credit institutions	7,067	-	-	-	-	-	-	7,067
Financial assets at amortised cost	-	-	-	-	4,000	-	-	4,000
Financial assets at fair value through other comprehensive income	-	-	-	-	-	-	344	344
Loans and advances to customers	23,588	1,935	14,842	26,581	9,881	2,073	-	78,900
Loans and term deposits due from credit institutions	-	400	-	-	-	-	-	400
Intangible assets	-	-	-	-	-	-	9	9
Property and equipment	-	-	-	-	-	-	758	758
Other assets	-	-	-	-	-	-	4,811	4,811
Total assets	110,675	2,335	14,842	26,581	13,881	2,073	12,461	182,848
Liabilities								
Deposits	134,718	4,842	6,895	12,074	10,029	-	-	168,558
Subordinated liabilities	-	1,500	-	-	1,471	427	-	3,398
Other financial liabilities	-	-	-	-	-	-	2,535	2,535
Total financial liabilities	134,718	6,342	6,895	12,074	11,500	427	2,535	174,491
Capital and reserves	-	-	-	-	-	-	8,357	8,357
Total liabilities, capital and reserves	134,718	6,342	6,895	12,074	11,500	427	10,892	182,848
Interest rate risk	(24,043)	(4,007)	7,947	14,507	2,381	1,646	1,569	-

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

32 INTEREST RATE REPRICING ANALYSIS (CONTINUED)

The interest rate repricing analysis of the Group's and the Bank's assets and liabilities as at 31 December 2017 was as follows:

Group

EUR'000	Less than 1 month	1 – 3 months	3 – 6 months	6 – 12 months	1 – 5 years	Over 5 years	Not sensitive to changes in interest rates	Total
Financial assets								
Cash and balances due from the Bank of Latvia	99,421	-	-	-	-	-	7,892	107,313
Demand deposits with credit institutions	21,429	-	-	-	-	-	-	21,429
Held-to-maturity assets	-	2,412	-	-	3,944	-	-	6,356
Available-for-sale financial assets	-	8,352	21,605	530	1,708	-	286	32,481
Loans (adjusted)	10,370	9,268	27,699	16,129	13,057	258	4	76,785
Loans and term deposits due from credit institutions	758	417	709	-	-	-	-	1,884
Intangible assets	-	-	-	-	-	-	28	28
Property and equipment	-	-	-	-	-	-	982	982
Investment property	-	-	-	-	-	-	15,196	15,196
Other assets	-	-	-	-	-	-	8,402	8,402
Total assets	131,978	20,449	50,013	16,659	18,709	258	32,790	270,856
Liabilities								
Deposits	204,832	4,852	8,371	16,546	14,821	-	-	249,422
Subordinated liabilities	-	-	285	1,900	2,491	707	-	5,383
Other financial liabilities	-	-	-	-	-	-	5,604	5,604
Total financial liabilities	204,832	4,852	8,656	18,446	17,312	707	5,604	260,409
Capital and reserves	-	-	-	-	-	-	10,447	10,447
Total liabilities, capital and reserves	204,832	4,852	8,656	18,446	17,312	707	16,051	270,856
Interest rate risk	(72,854)	15,597	41,357	(1,787)	1,397	(449)	16,739	-

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

32 INTEREST RATE REPRICING ANALYSIS (CONTINUED)

Bank

EUR'000	Less than 1 month	1 – 3 months	3 – 6 months	6 – 12 months	1 – 5 years	Over 5 years	Not sensitive to changes in interest rates	Total
Financial assets								
Cash and balances due from the Bank of Latvia	99,421	-	-	-	-	-	7,892	107,317
Demand deposits with credit institutions	21,429	-	-	-	-	-	-	21,429
Held-to-maturity assets	-	2,412	-	-	3,944	-	-	6,356
Available-for-sale financial assets	-	8,352	21,605	530	1,708	-	286	32,481
Loans	10,136	10,711	27,205	30,089	12,737	2,621	-	93,498
Loans and term deposits due from credit institutions	758	417	709	-	-	-	-	1,884
Intangible assets	-	-	-	-	-	-	28	28
Property and equipment	-	-	-	-	-	-	974	974
Other assets	-	-	-	-	-	-	6,042	6,043
Total assets	131,744	21,892	49,519	30,619	18,389	2,621	15,222	270,006
Liabilities								
Deposits	204,834	4,852	8,371	16,546	14,821	-	-	249,424
Subordinated liabilities	-	-	285	1,900	2,491	707	-	5,383
Other liabilities	-	-	-	-	-	-	5,336	5,355
Total liabilities	204,834	4,852	8,656	18,446	17,312	707	5,336	259,475
Capital and reserves	-	-	-	-	-	-	9,863	9,863
Total liabilities, capital and reserves	204,834	4,852	8,656	18,446	17,312	707	15,199	270,006
Interest rate risk	(73,090)	17,040	40,863	12,173	1,077	1,914	23	-

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

32 INTEREST RATE REPRICING ANALYSIS (CONTINUED)

Sensitivity analysis

The following demonstrates the sensitivity to reasonably possible changes in interest rates of the Bank's statement of comprehensive income. The analysis assumes that all other variables, in particular foreign currency rates, remain constant. The sensitivity of statement of comprehensive income is the effect of the assumed changes in the interest rates on the net interest income for one year, following the reporting period end date, based on the floating rate non-trading financial assets and financial liabilities held at 31 December 2018 and 31 December 2017.

Sensitivity of the Group's profit and loss to changes in interest rates is not disclosed separately as it does not differ significantly from that of the Bank.

An increase and decrease of interest rates by 100 basis points would result in the following change to the statement of comprehensive income and equity:

EUR'000	2018		2017	
	Profit or loss	Shareholders' equity	Profit or loss	Shareholders' equity
Increase in interest rates	(158)	0	(253)	(156)
Decrease in interest rates	158	0	253	158
Increase in USD interest rates	(68)	0	(116)	(153)
Decrease in USD interest rates	68	0	116	155

33 FINANCIAL ASSETS AND LIABILITIES BY CATEGORIES

Group 31 December 2018

	Financial assets at amortised cost	Financial assets and liabilities at fair value through profit or loss	Financial assets and liabilities at fair value through other comprehensive income	Loans and receivables	Liabilities at amortised cost	Total
EUR'000						
Financial assets						
Cash and balances due from the Bank of Latvia	-	-	-	86,559	-	86,559
Demand deposits with credit institutions	-	-	-	7,067	-	7,067
Financial assets at amortised cost	4,000	-	-	-	-	4,000
Financial assets at fair value through other comprehensive income	-	2	342	-	-	344
Loans and receivables	-	-	-	62,139	-	62,139
Other financial assets	-	-	-	6,593	-	6,593
Total financial assets	4,000	2	342	162,358	-	166,702
Financial liabilities						
Deposits	-	-	-	-	168,554	168,554
Subordinated liabilities	-	-	-	-	3,398	3,398
Other financial liabilities	-	-	-	-	1,981	1,981
Total financial liabilities	-	-	-	-	173,933	173,933

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

33 FINANCIAL ASSETS AND LIABILITIES BY TYPES (CONTINUED)

Bank 31 December 2018

	Held-to-maturity investments	Financial assets and liabilities designated at fair value through profit or loss	Financial assets and liabilities designated at fair value through other comprehensive income	Loans and receivables	Liabilities measured at amortised cost	Total
EUR'000						
Financial assets						
Cash and balances due from the Bank of Latvia	-	-	-	86,558	-	86,558
Demand deposits with credit institutions	-	-	-	7,067	-	7,067
Financial assets at amortised cost	4,000	-	-	-	-	4,000
Financial assets at fair value through other comprehensive income	-	2	342	-	-	344
Loans and receivables	-	-	-	79,300	-	79,300
Other financial assets	-	-	-	4,708	-	4,708
Total financial assets	4,000	2	342	177,633	-	181,977
Financial liabilities						
Deposits	-	-	-	-	168,554	168,554
Subordinated liabilities	-	-	-	-	3,398	3,398
Other financial liabilities	-	-	-	-	1,981	1,981
Total financial liabilities	-	-	-	-	173,933	173,933

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

33 FINANCIAL ASSETS AND LIABILITIES BY TYPES (CONTINUED)

Group 31 December 2017

	Held-to-maturity investments	Financial assets and liabilities designated at fair value through profit or loss	Financial assets and liabilities designated at fair value through other comprehensive income	Loans and receivables	Liabilities measured at amortised cost	Total
EUR'000						
Financial assets						
Cash and balances due from the Bank of Latvia	-	-	-	71,626	-	71,626
Demand deposits with credit institutions	-	-	-	33,140	-	33,140
Held-to-maturity investments	16,962	-	-	-	-	16,962
Available-for-sale financial assets	-	-	53,283	-	-	53,283
Loans and receivables	-	-	-	104,648	-	104,648
Other financial assets	-	-	-	5,739	-	5,739
Total financial assets	16,962	2	53,283	215,153	-	285,400
Financial liabilities						
Deposits	-	-	-	-	249,422	249,422
Subordinated liabilities	-	-	-	-	5,383	5,383
Other financial liabilities	-	-	-	-	3,537	3,537
Total financial liabilities	-	-	-	-	258,342	258,342

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

33 FINANCIAL ASSETS AND LIABILITIES BY TYPES (CONTINUED)

Bank 31 December 2017

	Held-to-maturity investments	Financial assets and liabilities designated at fair value through profit or loss	Financial assets and liabilities designated at fair value through other comprehensive income	Loans and receivables	Liabilities measured at amortised cost	Total
EUR'000						
Financial assets						
Cash and balances due from the Bank of Latvia	-	-	-	103,546	-	103,546
Demand deposits with credit institutions	-	-	-	21,429	-	21,429
Held-to-maturity investments	6,356	-	-	-	-	6,356
Available-for-sale financial assets	-	3	32,478	-	-	32,481
Loans and receivables	-	-	-	95,879	-	95,879
Other financial assets	-	-	-	5,905	-	5,905
Total financial assets	6,356	3	32,478	226,759	-	265,596
Financial liabilities						
Deposits	-	-	-	-	249,424	249,424
Subordinated liabilities	-	-	-	-	5,383	5,383
Other financial liabilities	-	-	-	-	3,537	3,537
Total financial liabilities	-	-	-	-	258,344	258,344

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

34 CURRENCY ANALYSIS

The Group and the Bank actively controls foreign exchange open positions. The Bank operates based on the Law on Credit Institutions stating that the open position in any currency should not exceed 10% of shareholders' equity and that the total open position should not exceed 20% of the shareholders' equity.

The currency analysis of the Group's and the Bank's expected and contingent liabilities as at 31 December 2018 was as follows:

Group

	EUR	USD	Others	Total
31 December 2018	EUR'000	EUR'000	EUR'000	EUR'000
Assets				
Cash and balances due from the Bank of Latvia	85,113	1150	296	86,559
Demand deposits with credit institutions	1,454	3,745	1,868	7,067
Financial assets at amortised cost	754	3,246	-	4,000
Financial assets at fair value through other comprehensive income	2	342	-	344
Loans and advances to customers	60,019	1,720	-	61,739
Loans and term deposits due from credit institutions	400	-	-	400
Intangible assets	9	-	-	9
Property and equipment	764	-	-	764
Investment property	15,807	-	-	15,807
Other assets	3,904	2,801	12	6,717
Total assets	168,226	13,004	2,176	183,406
Liabilities				
Deposits	143,193	21,368	3,993	168,554
Subordinated liabilities	3,398	-	-	3,398
Other financial liabilities	2,588	103	6	2,697
Provisions	53	-	-	53
Total liabilities	149,232	21,471	3,999	174,702
Capital and reserves	8,563	141	-	8,704
Total liabilities, capital and reserves	157,795	21,612	3,999	183,406
Net open position in the statement of financial position	10,457	(8,634)	(1,823)	-
Net position arising from currency exchange transactions	(10,300)	8,299	2,001	-
Total net open position	157	(335)	178	-

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

34 CURRENCY ANALYSIS (CONTINUED)

Bank

	EUR EUR'000	USD EUR'000	Others EUR'000	Total EUR'000
31 December 2018				
Assets				
Cash and balances due from the Bank of Latvia	85,113	1,149	296	86,558
Demand deposits with credit institutions	1,454	3,745	1,868	7,067
Financial assets at amortised cost	754	3,246	-	4,000
Financial assets at fair value through other comprehensive income	2	342	-	344
Loans and advances to customers	76,765	2,135	-	78,900
Loans and term deposits due from credit institutions	400	-	-	400
Intangible assets	9	-	-	9
Property and equipment	758	-	-	758
Other assets	1,996	2,804	12	4,812
Total assets	167,251	13,421	2,176	182,848
Liabilities				
Deposits	143,197	21,368	3,993	168,558
Subordinated liabilities	3,398	-	-	3,398
Other liabilities	2,373	103	6	2,482
Provisions	53	-	-	53
Total liabilities	149,021	21,471	3,999	174,491
Capital and reserves	8,216	141	0	8,357
Total liabilities, capital and reserves	157,237	21,612	3,999	182,848
Net open position in the statement of financial position	10,039	(8,216)	(1,823)	-
Net position arising from currency exchange transactions	(10,300)	8,299	2,001	-
Total net open position	(261)	83	178	-

The currency analysis of the Group's and the Bank's expected and contingent liabilities as at 31 December 2017 was as follows:

Group

	EUR EUR'000	USD EUR'000	Others EUR'000	Total EUR'000
As at 31 December 2017				
Assets				
Cash and balances due from the Bank of Latvia	105,955	890	467	107,312
Demand deposits with credit institutions	2,826	15,561	3,042	21,429
Held-to-maturity investments	3,698	34,853	-	38,551
Available-for-sale financial assets	-	283	-	283
Loans and advances to customers	73,890	2,895	-	76,785
Loans and term deposits due from credit institutions	-	1,884	-	1,884
Intangible assets	28	-	-	28
Property and equipment	982	-	-	982
Investment property	15,196	-	-	15,196
Other assets	7,987	414	2	8,403
Total assets	210,565	56,780	3,511	270,856
Liabilities				
Deposits	162,069	80,743	6,610	249,422
Subordinated liabilities	5,383	-	-	5,383
Other financial liabilities	4,734	710	159	5,603
Total liabilities	172,186	81,453	6,769	260,408
Capital and reserves	10,414	34	-	10,448

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Total liabilities, capital and reserves	182,600	81,487	6,769	270,856
Net open position in the statement of financial position	27,965	(24,707)	(3,258)	-
Net position arising from currency exchange transactions	(27,447)	23,997	3,450	-
Total net open position	518	(710)	192	-

34 CURRENCY ANALYSIS (CONTINUED)

Bank

	EUR EUR'000	USD EUR'000	Others EUR'000	Total EUR'000
As at 31 December 2017				
Assets				
Cash and balances due from the Bank of Latvia	105,955	890	467	107,312
Demand deposits with credit institutions	2,826	15,561	3,042	21,429
Held-to-maturity investments	3698	34,853	-	38,551
Available-for-sale financial assets	3	283	-	286
Loans and advances to customers	90,092	3,407	-	93,499
Loans and term deposits due from credit institutions	-	1884	-	1884
Intangible assets	28	-	-	28
Property and equipment	974	-	-	974
Other financial assets	5,627	414	2	6,043
Total financial assets	209,203	57,292	3,511	270,006
Liabilities				
Deposits	162,071	80,743	6,610	249,424
Subordinated liabilities	5,383	-	-	5,383
Other liabilities	4,487	710	159	5,356
Total financial liabilities	171,941	81,453	6,769	260,163
Capital and reserves	9,809	34	-	9,843
Total liabilities, capital and reserves	181,750	81,487	6,769	270,006
Net open position in the statement of financial position	27,453	(24,195)	(3,258)	-
Net position arising from currency exchange transactions	(27,447)	23,997	3,450	-
Total net open position	6	(198)	192	-

An analysis of sensitivity of the Group's and Bank's net income for the year and equity to changes in the foreign currency exchange rates based on positions existing as at 31 December 2018 and 2017 and a simplified scenario of a 10% change in USD to EUR exchange rates is as follows:

Group

EUR'000	2018	2017
	Net profit	Net profit
10% appreciation of USD against EUR	8	1
10% depreciation of USD against EUR	(8)	(1)

Bank

EUR'000	2018	2017
	Net profit	Net profit
10% appreciation of USD against EUR	(34)	5
10% depreciation of USD against EUR	34	(5)

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

35 MATURITY ANALYSIS OF ASSETS AND LIABILITIES

The below amounts represent the assets and liabilities grouped by residual maturity.

The Finance Operation Department based on its liquidity management policy manages liquidity risk. All departments whose operations affect the liquidity of the Group and the Bank are involved in liquidity management. The structure of assets/liabilities and the difference between them are calculated in order to carry out liquidity control. Liquidity is largely managed by using monetary instruments.

The Bank is active in managing its net liquidity position by means of:

- reducing maturities of assets, including by maintaining large balances on correspondent accounts or interbank overnight deposits and by investing funds in highly liquid debt securities in the available-for-sale portfolio or in highly liquid debt securities in the held-to-maturity portfolio, which are accepted as collateral by the ECB or other market players.
- increasing maturities of liabilities by attracting term deposits.

The Bank approves limits on net liquidity positions in general, as well as in EUR and USD.

As at 31 December 2018 and 31 December 2017 the individual liquidity coverage ratio for the Bank was 638% and 661%, respectively, and for the Group it was 639% and 658%, respectively.

The maturity analysis of the Bank's and the Group's assets and liabilities as at 31 December 2018 was as follows:

Group

	Up to 1 month including	1 to 3 months	3 to 6 months	6 to 12 months	More than 1 year	Over 5 years or not determined	Total
31 December 2018	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000
Assets							
Cash and balances due from the Bank of Latvia	86,559	-	-	-	-	-	86,559
Demand deposits with credit institutions	7,067	-	-	-	-	-	7,067
Financial assets at amortised cost	-	-	-	-	4,000	-	4,000
Financial assets at fair value through other comprehensive income	-	-	-	-	-	344	344
Loans and term deposits due from credit institutions	-	400	-	-	-	-	400
Loans and advances to customers	5,146	1,198	1,904	9,316	18,996	25,179	61,739
Intangible assets	-	-	-	-	-	9	9
Property and equipment	-	-	-	-	-	764	764
Investment property	-	-	-	-	-	15,807	15,807
Other assets	6,717	-	-	-	-	-	6,717
Total assets	105,489	1,598	1,904	9,316	22,996	42,103	183,406
Liabilities							
Deposits	123,348	4,842	6,930	12,074	10,034	11,326	168,554
Subordinated liabilities	-	1,500	-	-	1,471	427	3,398
Other liabilities	2,750	-	-	-	-	-	2,750
Total liabilities	126,098	6,342	6,930	12,074	11,505	11,753	174,702
Capital and reserves	-	-	-	-	-	8,704	8,704
Total capital, liabilities and reserves	126,098	6,342	6,930	12,074	11,505	20,457	183,406
Liquidity risk	(20,609)	(4,744)	(5,026)	(2,758)	11,491	21,646	-

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

35 MATURITY ANALYSIS OF ASSETS AND LIABILITIES (CONTINUED)

Bank

	Up to 1 month including	1 to 3 months	3 to 6 months	6 to 12 months	More than 1 year	Over 5 years or not determine d	Total
31 December 2018	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000
Financial assets							
Cash and balances due from the Bank of Latvia	86,559	-	-	-	-	-	86,559
Demand deposits with credit institutions	7,067	-	-	-	-	-	7,067
Financial assets at amortised cost	-	-	-	-	4,000	-	4,000
Financial assets at fair value through other comprehensive income	-	-	-	-	-	344	344
Loans and term deposits due from credit institutions	-	400	-	-	-	-	400
Loans and advances to customers	5,341	1,281	2,780	26,784	17,639	25,075	78,900
Intangible assets	-	-	-	-	-	9	9
Property and equipment	-	-	-	-	-	758	758
Other assets	4,811	-	-	-	-	-	4,811
Total assets	103,778	1,681	2,780	26,784	21,639	26,186	182,848
Liabilities							
Deposits	123,352	4,842	6,930	12,074	10,034	11,326	168,558
Subordinated liabilities	-	1,500	-	-	1,471	427	3,398
Other liabilities	2,535	-	-	-	-	-	2,535
Total liabilities	125,887	6,342	6,930	12,074	11,505	11,753	174,491
Capital and reserves	-	-	-	-	-	8,357	8,357
Total capital, liabilities and reserves	125,887	6,342	6,930	12,074	11,505	20,110	182,848
Liquidity risk	(22,109)	(4,661)	(4,150)	14,710	10,134	6,076	-

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

35 MATURITY ANALYSIS OF ASSETS AND LIABILITIES (CONTINUED)

The maturity analysis of the Bank's assets and liabilities as at 31 December 2017 was as follows:

Group

	Up to 1 month including	1 to 3 months	3 to 6 months	6 to 12 months	More than 1 year	Over 5 years or not determine d	Total
As at 31 December 2017	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000
Financial assets							
Cash and balances due from the Bank of Latvia	107,313	-	-	-	-	-	107,313
Demand deposits with credit institutions	21,429	-	-	-	-	-	21,429
Held-to-maturity investments	-	2,412	-	-	3,944	-	6,356
Available-for-sale financial assets	32,195	-	-	-	-	286	32,481
Loans and term deposits due from credit institutions	758	417	-	-	709	-	1,884
Loans and advances to customers	5,186	3,214	11,649	20,424	23,786	12,526	76,785
Intangible assets	-	-	-	-	-	28	28
Property and equipment	-	-	-	-	-	982	982
Investment property	-	-	-	-	-	15,196	15,196
Other financial assets	8,402	-	-	-	-	-	8,402
Total assets	175,283	6,043	11,649	20,424	28,439	29,018	270,856
Financial liabilities							
Deposits	193,238	4,923	8,381	16,572	14,982	11,326	249,422
Subordinated liabilities	-	-	285	1,900	2,491	707	5,383
Other financial liabilities	5,563	-	-	-	41	-	5,604
Total financial liabilities	198,801	4,923	8,666	18,472	17,514	12,033	260,409
Capital and reserves	-	-	-	-	-	10,447	10,447
Total capital, liabilities and reserves	198,801	4,923	8,666	18,472	17,514	22,480	270,856
Liquidity risk	(23,327)	1,120	2,983	1,952	11,421	5,851	-

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

35 MATURITY ANALYSIS OF ASSETS AND LIABILITIES (CONTINUED)

Bank

	Up to 1 month including	1 to 3 months	3 to 6 months	6 to 12 months	More than 1 year	Over 5 years or not determine d	Total
As at 31 December 2017	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000
Assets							
Cash and balances due from the Bank of Latvia	107,313	-	-	-	-	-	107,313
Demand deposits with credit institutions	21,429	-	-	-	-	-	21,429
Held-to-maturity investments	-	2,412	-	-	3,944	-	6,356
Available-for-sale financial assets	32,195	-	-	-	-	286	32,481
Loans and term deposits due from credit institutions	758	417	-	-	709	-	1,884
Loans and advances to customers	5,544	4,654	11,265	35,046	24,465	12,524	93,498
Intangible assets	-	-	-	-	-	28	28
Property and equipment	-	-	-	-	-	974	974
Other assets	6,043	-	-	-	-	-	6,043
Total assets	173,282	7,483	11,265	35,046	29,118	13,812	270,006
Liabilities							
Deposits	193,240	4,923	8,381	16,572	14,982	11,326	249,424
Subordinated liabilities	-	-	285	1,900	2,491	707	5,383
Other liabilities	5,295	-	-	-	41	-	5,336
Total liabilities	198,535	4,923	8,666	18,472	17,514	12,033	260,143
Capital and reserves	-	-	-	-	-	9,863	9,863
Total capital, liabilities and reserves	198,535	4,923	8,666	18,472	17,514	21,896	270,006
Liquidity risk	(25,253)	2,560	2,599	16,574	11,604	(8,084)	-

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

35 MATURITY ANALYSIS OF ASSETS AND LIABILITIES (CONTINUED)

Analysis of financial liabilities' contractual undiscounted cash flows.

The table below presents the cash flows payable by the Bank under both non-derivative and derivative financial liabilities by remaining contractual maturities as at 31 December 2018 and 2017.

The amounts disclosed in the table are the contractual undiscounted cash flows in comparison with carrying amounts of financial liabilities, comprising discounted cash flows as at the reporting date.

The Group analysis of financial liabilities' contractual undiscounted cash flows has not been presented as the differences to the Bank analysis are insignificant.

	Carrying amount	Gross nominal out flow	Less than 1 month	1 – 3 months	3 months to 1 year	1-5 years	Over 5 years
31 December 2018	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000
Deposits	(168,558)	(174,561)	(128,396)	(5,475)	(16,888)	(23,802)	-
Subordinated liabilities	(3,398)	(4,047)	-	-	(79)	(3,417)	(552)
Other financial liabilities	(1,981)	(1,981)	(1,981)	-	-	-	-
Total non-derivative financial liabilities	(173,937)	(52,367)	(2,155)	(5,475)	(16,967)	(27,219)	(552)
Loans and credit line liabilities	(1,299)	(1,299)	(1,299)	-	-	-	-
Guarantees and letters of credit	(1,590)	(1,590)	(40)	-	(1,544)	(6)	-
Total financial liabilities	(176,826)	(55,256)	(3,464)	(5,475)	(18,511)	(27,225)	(552)
	Carrying amount	Gross nominal inflow / (outflow)	Less than 1 month	1 – 3 months	3 months to 1 year	1-5 years	Over 5 years
As at 31 December 2017	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000	EUR'000
Non-derivative financial liabilities							
Deposits	(249,424)	(250,744)	(208,894)	(4,989)	(27,537)	(9,324)	-
Subordinated liabilities	(5,383)	(5,383)	-	-	(2,185)	(2,491)	(707)
Other financial liabilities	(3,537)	(3,537)	(3,537)	-	-	-	-
Total non-derivative financial liabilities	(258,344)	(259,664)	(212,431)	(4,989)	(29,722)	(11,815)	(707)
Loans and credit line liabilities	(4,354)	(4,354)	(4,354)	-	-	-	-
Guarantees and letters of credit	(756)	(756)	(6)	-	(709)	(41)	-
Total financial liabilities	(263,454)	(264,774)	(216,791)	(4,989)	(30,431)	(11,856)	(707)

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

36 CAPITAL ADEQUACY

The capital requirement for the Group and the Bank is set and monitored by the Financial and Capital Market Commission. Capital is defined by the Group and the Bank as items defined by statutory regulation as capital. Under the current capital requirements set by Financial and Capital Market Commission, banks must maintain a ratio of capital to risk weighted assets ("statutory capital ratio") above the prescribed minimum level. Furthermore, according to Section 35.25 of the Credit Institution Law, the Bank is required to ensure that its Tier 1 basic capital is sufficient to meet the total capital buffer requirement which given the provisions of Section 35.3(1) of the Credit Institution Law is comprised of a capital conservation buffer of 2.5% of total exposures calculated according to Article 92(3) of the Regulation and, as required in Section 35.4(1) of the Credit Institutions Law, of the specific countercyclical capital buffer (CCyB) calculated by multiplying the total value of exposures as required by Article 92(3) of the Regulation and the CCyB rate specific for the particular credit institution.

As at 31 December 2018 the individual minimum level is 13.5% which is increased by the total capital buffer requirement of 2.5% calculated as the sum of the capital buffer and the countercyclical capital buffer specific for the particular credit institution (31 December 2017: 10.2% which is increased by the total capital buffer requirement of 2.5% calculated as the sum of the capital buffer and the countercyclical capital buffer specific for the particular credit institution).

The actual capital adequacy ratio of the Group and the Bank was below the individual capital adequacy ratio set by the FCMC in the reporting years ended 31 December 2018 and 31 December 2017.

In order to achieve compliance with the total capital reserve requirements the Bank takes measures to strengthen capital as described in Note 40.

The following table shows the composition of the Group's capital position as at 31 December 2018 and 31 December 2017:

	31 December 2018 EUR'000	31 December 2017 EUR'000
Tier 1		
Share capital	15,999	15,651
Share premium	260	260
Reserve capital	4,155	4,155
Retained earnings/(accumulated loss) carried forward from previous years	(12,493)	(4,237)
Profit/ (loss) for the reporting year	42	(6,363)
Revaluation reserve of financial assets at FVOCI	141	18
Additional value adjustment	0	(1)
Intangible assets	(9)	(28)
Result of transition period conditions	1,799	-
Total Tier 1 capital	9,894	9,455
Tier 2 capital		
Subordinated capital (unamortised part)	1,630	2,290
Total Tier 2 capital	1,630	2,290
Statutory deductions from Tier 1 and Tier 2 capital	(261)	(320)
Total shareholders' equity	11,263	11,425
Risk weighted value of exposures to credit risk, counterparty credit risk, impairment of recoverable amounts and unpaid deliveries risk	100,205	109,143
Total exposure to position risk, foreign currency risk and commodity risk	614	927
Total exposure to operational risk	17,994	17,134
Total exposure to credit value adjustment risk	53	-
Total risk exposure	118,866	127,204
Total capital adequacy ratio	9.48%	8.98%
Minimum capital adequacy ratio set by the FCMC	13.50%	10.20%
Minimum capital adequacy ratio set by the FCMC including the total reserve requirement	16.00%	12.70%

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

The following table shows the composition of the Bank's capital position as at 31 December 2018 and 31 December 2017:

	31 December 2018 EUR'000	31 December 2017 EUR'000
Tier 1		
Share capital	15,999	15,651
Share premium	260	260
Reserve capital	4,155	4,155
Retained earnings of the previous years	(13,097)	(3,305)
Profit/ (loss) for the reporting year	300	(7,900)
Revaluation reserve of AFS other financial assets	141	17
Additional value adjustment	0	(1)
Intangible assets	(9)	(28)
Result of transition period conditions	1,798	-
Total Tier 1 capital	9,547	8,849
Tier 2 capital		
Subordinated capital (unamortised part)	1,630	2,290
Total Tier 2 capital	1,630	2,290
Statutory deductions from Tier 1 and Tier 2 capital	(261)	(320)
Total shareholders' equity	10,916	10,819
Risk weighted value of exposures to credit risk, counterparty credit risk, impairment of recoverable amounts and unpaid deliveries risk	99,384	107,927
Total exposure to position risk, foreign currency risk and commodity risk	387	298
Total exposure to operational risk	17,809	17,055
Total exposure to credit value adjustment risk	53	
Total risk exposure	117,634	125,280
Total capital adequacy ratio	9.28%	8.64%
Minimum capital adequacy ratio set by the FCMC	13.50%	10.20%
Minimum capital adequacy ratio set by the FCMC including the total reserve requirement	16.00%	12.70%

The risk-weighted assets are measured by means of a hierarchy of risk weights classified according to the nature of – and reflecting an estimate of credit, market and other risks associated with – each asset and counterparty, taking into account any eligible collateral or guarantees. A similar treatment is adopted for off-balance sheet exposure, with some adjustments to reflect the more contingent nature of the potential losses. The additional value adjustment was calculated according to the simplified approach based on Commission Delegated Regulation (EU) 2016/101.

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Capital adequacy ratio of the Group and the Bank without applying transitional regulations:

	31 December 2018	31 December 2017
	EUR'000	EUR'000
	Bank	Group
Tier 1 capital	7,750	8,096
Tier 2 capital	1,630	1,630
Statutory deductions from Tier 1 and Tier 2 capital	(261)	(261)
Total capital, fully loaded	9,119	9,465
Total risk exposure amount, fully loaded	115,570	116,938
Capital adequacy ratio, fully loaded	7,89%	8,09%

The above information is based on the Bank's and the Group's internal reports that are submitted to the Bank's management.

37 MAXIMUM CREDIT RISK EXPOSURE

The table below shows the maximum credit risk for the components of the statement of the financial position, including derivatives. Credit risk exposure is disclosed based on subjected to credit risk net carrying amount of statement of financial position items less doubtful loans and receivables.

The maximum credit exposures are shown gross, i.e. without taking into account any pledges and collaterals. Detailed information on the type and amount of collateral is presented in the note 11.

	Maximum credit exposure of the Group	
	2018	2017
Balances with the Bank of Latvia	80,020	99,421
Demand deposits with credit institutions	7,067	21,429
Held-to-maturity investments	-	6,356
Investments classified as available for sale	-	32,481
Financial instruments at amortised cost	4,000	-
Financial instruments at fair value through other comprehensive income	344	-
Loans and term deposits due from credit institutions	400	1,884
Loans and advances to customers	61,739	76,785
Other financial assets	6,593	8,239
Total items of the statement of financial position subjected to credit risk	160,163	246,595
Loans and credit line liabilities	1,299	4,354
Guarantees and letters of credit	1,590	756
Forecasted and contingent liabilities	2,889	5,110
Total maximum credit risk exposure	163,052	251,705

As it is shown above, 40 % from total gross maximum credit risk amount refers to loans and receivables (2017: 35%).

	Maximum credit exposure of the Bank	
	2018	2017
Balances with the Bank of Latvia	80,020	99,421
Demand deposits with credit institutions	7,067	21,429
Held-to-maturity investments	-	6,356
Investments classified as available for sale	-	32,481
Financial instruments at amortised cost	4,000	-
Financial instruments at fair value through other comprehensive income	344	-
Loans and term deposits due from credit institutions	400	1,884

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Loans and advances to customers	78,900	93,498
Other financial assets	4,708	5,905
Total items of the statement of financial position subjected to credit risk	175,439	260,974
Loans and credit line liabilities	1,299	4,354
Guarantees and letters of credit	1,590	756
Forecasted and contingent liabilities	2,889	5,110
Total maximum credit risk exposure	178,328	266,084

38 FAIR VALUE OF FINANCIAL INSTRUMENTS

(a) Financial instruments measured at fair value

The table below analyses the financial instruments of the Group and the Bank measured at fair value at the end of the reporting period, by the level in the fair value hierarchy into which the fair value measurement is categorised.

	Level 1: EUR'000	Level 2: EUR'000	Level 3: EUR'000	Total EUR'000
2018				
Financial assets				
Financial instruments at fair value through other comprehensive income	-	344	-	344
Total	-	344	-	344
2017				
Financial assets				
Available for sale financial assets	-	32,481	-	32,481
Total	-	32,481	-	32,481

(b) Financial instruments not measured at fair value

The table below analyses the fair values of the financial instruments of the Group and the Bank other than measured at fair value by the level in the fair value hierarchy into which each fair value measurement is categorised.

Group

	Level 1: EUR'000	Level 2: EUR'000	Level 3: EUR'000	Total fair value EUR'000	Total carrying amount EUR'000
31 December 2018					
Financial assets					
Cash and due from central banks	-	-	-	86,559	86,559
Demand deposits with credit institutions	-	-	7,067	7,067	7,067
Loans and advances to customers	-	-	62,139	62,139	62,139
Financial assets at amortised cost	-	4,112	-	4,112	4,000
Other financial assets	-	-	6,593	6,593	6,593
Financial liabilities					
Deposits	-	-	168,558	168,558	168,558
Other loans	-	-	3,398	3,398	3,398
Other liabilities	-	-	1,981	1,981	1,981
31 December 2017					
Financial assets					
Cash and due from central banks	-	-	-	107,313	107,313
Demand deposits with credit institutions	-	-	21,429	21,429	21,429
Loans and advances to customers	-	-	78,669	78,669	78,669
Held to maturity financial instruments	-	6,597	-	6,597	6,356
Other financial assets	-	-	8,239	8,239	8,239
Financial liabilities					

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Deposits	-	-	249,424	249,424	249,424
Other loans	-	-	5,383	5,383	5,383
Other liabilities	-	-	3,537	3,537	3,537

Bank

31 December 2018	Level 1: EUR'000	Level 2: EUR'000	Level 3: EUR'000	Total fair value EUR'000	Total carrying amount EUR'000
Financial assets					
Cash and due from central banks	-	-	-	86,559	86,559
Demand deposits with credit institutions	-	-	7,067	7,067	7,067
Loans and advances to customers	-	-	79,300	79,300	79,300
Financial assets at amortised cost	-	4,112	-	4,112	4,000
Other financial assets	-	-	4,708	4,708	4,708
Financial liabilities					
Deposits	-	-	168,558	168,558	168,558
Other loans	-	-	3,398	3,398	3,398
Other liabilities	-	-	1,981	1,981	1,981
31 December 2017					
	Level 1: EUR'000	Level 2: EUR'000	Level 3: EUR'000	Total fair value EUR'000	Total carrying amount EUR'000
Financial assets					
Cash and due from central banks	-	-	-	107,313	107,313
Demand deposits with credit institutions	-	-	21,429	21,429	21,429
Loans and advances to customers	-	-	95,382	95,382	95,382
Held to maturity financial instruments	-	6,597	-	6,597	6,356
Other financial assets	-	-	5,905	5,905	5,905
Financial liabilities					
Deposits	-	-	249,424	249,424	249,424
Other loans	-	-	5,383	5,383	5,383
Other liabilities	-	-	3,537	3,537	3,537

39 LITIGATIONS

In the ordinary course of business the Bank and the Group are subject to legal actions and complaints. Management believes that the ultimate liability, if any, arising from such actions or complaints, will not have a material adverse effect on the financial conditions of the results of future operations of the Group or the Bank.

40 GOING CONCERN

As disclosed in Note 36, in the year ended 31 December 2018, the Group and the Bank were not in compliance with the total individual capital adequacy requirement as set by the regulator. In addition, the situation at the end of the reporting period made the Group's and the Bank's capital adequacy ratio substantially sensitive to any possible additional decrease in capital.

The termination of operations of one of the largest Latvian privately owned banks provoked wide response and adversely affected reputation of the Latvian financial sector. In the 2nd quarter of 2018, amendments were introduced in regulations to prohibit servicing the so-called 'shell arrangements' where the legal person is not related to any actual business activity and the activity of the legal person involves little or no economic activity. As a result, during 2018 Latvian financial sector was pushed to go through fast and significant changes, which also significantly affected the Bank's existing business model and future operations at that time.

In the beginning of 2019 the Bank developed new strategy and worked out detailed business plan for the three years' period until 2021. The strategy includes the change of business model with the following directions:

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

- The Bank's transformation into mainly residents serving credit institution during 2019;
- Actively resume conventional banking operations primarily focusing on new lending to SME in Latvia and Lithuania;
- Strengthening the Bank's position as a niche merchant banking services provider for SME in Latvia and Lithuania.

The activities to be carried out are identified in the following work-streams:

- Strengthening of capital base;
- Strengthening the corporate governance and management team;
- Cost-cutting measures;
- Continued de-risking of client base;
- Non-performing assets recovery;
- Resume active banking operation and marketing activities.

Within the business model, the shareholders of the Bank have made a decision to attract a strategic investor for the Bank's capital by cooperating with a professional external consultant. In December 2018, the changes were made to the Bank's shareholding structure: a new minority shareholder SIA „J.A. Finance Holdings” (Latvia) held 100% by a Latvian citizen Jurijs Adamovičs joined the Bank.

In line with new strategy and business plan, one of the significant activities is strengthening the corporate governance starting with the top level of corporate governance in the Bank. Therefore on 10 December 2018, in an extraordinary shareholders' meeting the new Supervisory Board of the Bank was elected, setting 27 December 2018 as the first day of the authority of the new Supervisory Board. Jurijs Adamovičs, Ivars Grunte and Goča Tutberidze were elected as Supervisory Board members. The new constitution of the Supervisory Board is ensuring the best combination of individual competencies and suitability. Mr Adamovičs is a competent and internationally recognised professional specialising in the field of restructuring, recovery of companies and change management, setting the preparation of the Bank for the attraction of a strategic investor as his key priority. The election of Mr Grunte, the lead partner at TGS Baltics and a Member of the Latvian Collegium of Sworn Advocates, as a member of the Supervisory Board is a clear signal to the market players of the Bank's intent to strengthen its internal corporate governance processes and ensure the operation of the principle and system of the prevention of independent conflicts of interests. The role of Mr Tutberidze as a member of the Supervisory Board is to ensure succession of changes to be implemented within the restructuring of the Bank, supervising the management of specific risks pertaining to the Bank's operations and demonstrate stability to the Bank's long-term partners and customer base. Mr Tutberidze resigned in May 2019. The process of election of new Supervisory Board has started by asking all qualifying shareholders to submit their preferred candidates for the role of the Supervisory Board members to be evaluated in accordance with Bank's internal valuation procedures.

Further on, the changes to the Management Board took place at the beginning of 2019. On 3 January 2019 new Chairwoman of the Management Board, Solvita Deglava was elected. After resignation of Member of the Management Board Ilze Pudiste, on 25 February 2019 Ruta Amtmane was elected as a Member of the Management Board whose responsibilities are legal and AML matters. It is planned to expand the Management Board to four members.

On 6 February 2019 the capital strengthening activities plan was submitted to regulator consisting of eight steps to be carried out ensure the requirement of capital adequacy level is met by the Bank until end of 2019. Since then the Bank has been regularly informing the regulator on the status and execution of the submitted plan.

Cost-cutting measures will give positive effect on profit and loss statement after the completion of the transformation process, which amongst the others, include revisiting all the business processes aiming at more efficient and cost effective performance.

During 2018, the Bank gradually terminated cooperation with 'shell arrangements', thus 735 accounts of customers who met the definition of the new AML/TF law were closed. However, the Bank preserved such customers who do not meet several criteria as included in the laws and regulations of the Republic of Latvia. The proportion of such customers in 2018 is lower than 10% and the Bank plans to terminate business relationships with the majority by the end of June 2019. As a result of these measures, a one-off increase in income from commission and foreign currency exchange transactions was observed in 2018 up to forecasted EUR 10 million and EUR 2,5 million respectively, however the amount of this income for 2019 is expected considerably lower.

During 2019 the Bank actively started to take measures to improve the quality of its loan portfolio, incl. restructuring and legal recovery and sale, as well as approved and started to realise gradual sales plan of investment properties owned by the Group's subsidiary, thus freeing up funds for investing in the higher quality loan products.

Following these activities the Group and the Bank plan to increase profitability as of 2019 and expects to be in compliance with the total individual capital adequacy requirement set by the regulator by the end of 2019.

NOTES TO THE BANK'S SEPARATE AND GROUP'S CONSOLIDATED FINANCIAL STATEMENTS

Based on above, the Management of the Group and the Bank conclude that the going concern principle is applicable to the preparation of these separate and consolidated financial statements. However, a material uncertainty still exists that may cast doubt on the Group's and the Bank's ability to continue as a going concern. The key sources of uncertainty include:

- potential future results of the reviews and regulatory reviews at the Bank in the field of AML/TF/Sanctions, including the potential amount of the fines, considering reviews carried out by the regulator in the banking sector since 2015;
- the further risks arising from the Bank's inability to comply with the regulatory requirements of the maximum credit risk concentration with one customer or a group of related customers as at 31 December 2018 should the Bank fail to ensure the completion of capital strengthening activities.
- the amount of the overall current and future regulatory changes affecting the financial sector of the Republic of Latvia, as well as the Bank's and the Group's ability to implement measures and agree upon them with the regulator to mitigate regulatory, compliance and reputational risk in the corresponding period. As great uncertainty governs the regulatory environment, the extended amount of limitations in relation to the provision of services to certain international customer categories may cause further adverse consequences to the Bank's and the Group's operation. Should the regulatory environment change differently from the original initiatives, the Bank has to review its strategy again.
- The Bank's and the Group's ability to implement the new strategy and business plan, develop the customer base with acceptable risk profile, generate profit and maintain the regulatory capital adequacy in the transition period. Financial success will depend on the Bank's ability to implement changes in corporate governance and management, as well as on the Bank's and the Group's current and potential shareholders' ability to invest the necessary additional share capital for the maintenance of future operations.

41 SUBSEQUENT EVENTS

On 7 January, 2019, the new Council and the Management board of AS Meridian Trade Bank has been registered in the Register of Enterprises of the Republic of Latvia. According to the Articles of Association of AS Meridian Trade Bank, the Council and the Management board have been elected for five years.

In February 2019, AS Meridian Trade Bank's representative office in Moscow has ceased its operations.

Except for the above, there have been no events that would have to be reflected in these financial statements for the period since the end of the reporting year.



Translation from Latvian original*

INDEPENDENT AUDITOR'S REPORT

To the shareholders of AS Meridian Trade Bank

Report on the audit of the consolidated and separate financial statements

Our opinion

In our opinion, the separate financial statements of AS Meridian Trade Bank (the "Bank") and the consolidated financial statements of the Bank and its subsidiaries (the "Group") set out on pages 8 to 82 of the accompanying annual report, give a true and fair view of the financial position of the Group and the Bank as at 31 December 2018, and of the financial performance and the cash flows of the Group and the Bank for the year then ended in accordance with the International Financial Reporting Standards as adopted by the European Union (IFRSs).

What we have audited

The Group's consolidated and the Bank's separate financial statements comprise:

- the Bank's separate and Group's consolidated statement of financial position as at 31 December 2018;
- the Bank's separate and Group's consolidated statement of profit or loss and other comprehensive income for the year then ended;
- the Bank's separate and Group's consolidated statement of changes in shareholder's equity for the year then ended;
- the Bank's separate and Group's consolidated statement of cash flows for the year then ended; and
- the notes to the Bank's separate and Group's consolidated financial statements, which include the significant accounting policies.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing adopted in the Republic of Latvia (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the Consolidated and Separate financial statements* section of our report.

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

Independence

We are independent of the Group and the Bank in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code) and with the ethical requirements and auditor's independence rules that are relevant to our audit of the consolidated and separate financial statements in Latvia. We have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

We have not provided non-audit services to the Group and the Bank in the period from 1 January 2018 to 31 December 2018.

Material uncertainty related to going concern

We draw attention to “Going concern considerations” set out in Note 40 of the financial statements, which indicate material uncertainties related to the Bank’s need to ensure its individually determined capital level, execute the capital strengthening plan agreed with the Bank Regulator including implementing a revised strategy to replace a significant part of its non-resident customer business in response to recent changes in the Law on the Prevention of Money Laundering and Terrorism and Proliferation Financing of the Republic of Latvia. This, along with other matters as described in Note 40, indicates that a material uncertainty exists that may cast significant doubt on the Bank’s and the Group’s ability to continue as a going concern. Our opinion is not modified in respect of this matter.

Our audit approach

Overview



Overall Group and Bank materiality is EUR 171 thousand, which represents approximately 5% of average of absolute amount of profit or loss before tax of the Group for the past three years.

We conducted audit work in relation to separate financial information of the Bank.

We conducted audit work in relation to the material balances and transactions of the other subsidiaries of the Bank included in the consolidation group as at 31 December 2018.

- Fair value of investment properties (the Group).
 - Expected credit losses on loans (the Group and the Bank).
-

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the consolidated and separate financial statements (together “the financial statements”). In particular, we considered where management made subjective judgements; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. We also addressed the risk of management override of internal controls, including among other matters, consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

Materiality

The scope of our audit was influenced by our application of materiality. An audit is designed to obtain reasonable assurance whether the financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if

* This version of our report is a translation from the original, which was prepared in Latvian. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation.

individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall Group and Bank materiality for the consolidated and separate financial statements as a whole as set out in the table below. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Overall Group and Bank materiality	Overall materiality applied to the Group and the Bank was EUR 171 thousand.
How we determined it	5% of average of absolute amount of profit or loss before tax of the Group for the past three years.
Rationale for the materiality benchmark applied	<p>We chose average of absolute amount of profit or loss before tax for the past three years as the benchmark because, in our view, it is the benchmark, which is of primary focus by the users of the financial statements.</p> <p>We chose 5%, which, based on our judgment, is within the range of acceptable quantitative materiality thresholds.</p>

We agreed with the Audit Committee that we would report to them the misstatements identified during our audit above EUR 8.5 thousand, as well as the misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. In addition to the matters described in the *Material uncertainty related to going concern* section above, we have determined the matters described below to be the key audit matters to be communicated in our report.

Key audit matters	How our audit addressed the key audit matter
<p>Fair value of investment properties (the Group)</p> <p>Refer to Note 13 <i>‘Investment property’</i> of the consolidated financial statements.</p> <p>Investment property as per consolidated financial statements mainly comprise underlying investment property held by the subsidiaries of the Bank.</p>	<p>We assessed that the Group’s accounting policies in relation to the fair valuation of investment properties are based on IFRS requirements.</p> <p>We tested that upon consolidation the investment properties owned by the subsidiaries of the Bank have been recognised in the consolidated balance sheet as at 31 December 2018.</p>

* This version of our report is a translation from the original, which was prepared in Latvian. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation.

We focused on this area because the management makes subjective judgements when determining the fair value of investment properties, especially where the properties are of a type and location in which currently there is limited or no active market. Therefore, a variety of valuation techniques are used with inputs that are observable in the market and inputs that are not observable in the market.

The management obtains reports from certified independent appraisers to assist them in determining the properties' fair values. Based on the type of investment property various valuation methods are used – market evidence of transaction prices for similar properties, income method or discounted cash flow method.

The most significant judgements made by the management in respect of fair valuation of investment properties are comparative market prices and discounted cash flows, including rent rates, expenses, growth rate, etc.

For a selected sample of investment properties, we reviewed the independent valuations the Group obtained in respect of the underlying investment properties. We involved our valuation specialists in order to perform this assessment.

Where comparative market data was used, we evaluated whether the location, condition and other relevant attributes of the property are similar to those of the comparable assets used by valuers.

Where valuation models were used, we evaluated the reasonableness of inputs into the valuation models – future cash flows, growth rates, discount rates.

We also performed our own search of comparable market data, as well as assessed the calculation of fair values using discounted future cash flow models where it was considered necessary.

We verified the disclosures in the financial statements in respect of investment properties.

Expected credit losses on loans (the Group and the Bank)

Refer to Note 11 '*Loans*' to the consolidated and separate financial statements.

We focused on this area because management has adopted IFRS 9 "Financial instruments" in 2018 and implemented expected credit loss (ECL) model for loan impairment losses. Management makes complex and subjective judgements over the estimation of the ECL. The key features of the ECL model include classification of loans into 3 stages, assessment of credit risk parameters and application of forward looking information.

The amount of ECL for the Group's and Bank's loans is based on the model calculations taking into consideration the exposure at default, probability of default, changes in customer credit rating, other known risk factors impacting stage of each exposure, and taking into account estimated future cash flows from the loan

We assessed that the Group's and Bank's accounting policies in relation to the ECL of loans to customers are based on requirements of IFRS 9 by assessing each significant model component: exposure at default, probability of default and loss given default, definitions of default and significant increase in credit risk, use of macroeconomic scenarios.

Further, on a sample basis we performed detailed testing over reliability of loan data, including contract dates, interest rates, collateral values and types, performing/ non-performing status and other inputs used in ECL calculation.

For a sample of loans, we evaluated reasonableness of assumptions related to future expected cash flows and recoverability of loans as made by credit expert for individually assessed loans. We have verified the rationale of these assumptions and verified the reasonableness of the values of collateral used in the assessment.

* This version of our report is a translation from the original, which was prepared in Latvian. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation.

repayments or sale of collateral (loss given default), and ECL adjustments by expected impact of future macroeconomic scenarios.

For all loans in Stage 1 and 2 the expected credit losses are calculated using the ECL model, while for all exposures in Stage 3 expected credit losses are calculated on individual basis.

IFRS 9 adoption as at 1 January 2018 resulted in decrease of the Group's and Bank's equity by EUR 1,662 thousand due to re-measurements of loans. Net result for expected credit losses for the year ended 31 December 2018 amounted to the loss of EUR 2,816 thousand for the Group and EUR 2,826 for the Bank.

On a sample basis, we tested the collectively assessed credit loss allowance for loans to customers. We analyzed PD, LGD and EAD used by the Bank. We recalculated the final credit loss allowance for loans and advances assessed on collective basis using the ECL model.

How we tailored our Group audit scope

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the consolidated and separate financial statements as a whole, taking into account the structure of the Group, the accounting processes and controls, and the industry in which the Group operates.

Audit work in relation to the consolidated and separate financial statements was performed by the Group engagement team and no component auditors were involved. Our audit scope covered 99% of profit for the year and 99% of total assets of the Group.

Reporting on other information including the Management Report

Management is responsible for the other information. The other information comprises:

- Management Report as set out on pages 3 to 5 of the accompanying Annual Report;
- Information on the Bank's Management as set out on page 6 of the accompanying Annual Report;
- Statement of Responsibility of the Bank's Management as set out on page 7 of the accompanying Annual Report;

(but does not include the financial statements and our auditor's report thereon), which we obtained prior to the date of this auditor's report.

Our opinion on the consolidated and separate financial statements does not cover the other information, including the Management Report, Information on the Bank's Management and Statement of Responsibility of the Bank's Management.

In connection with our audit of the consolidated and separate financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated and separate financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

* This version of our report is a translation from the original, which was prepared in Latvian. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation.



With respect to the Management Report, we also performed the procedures required by Law on Audit Services. Those procedures include considering whether the Management Report is prepared in accordance with the requirements of the applicable legislation.

Based on the work undertaken in the course of our audit, in our opinion, in all material respects:

- the information given in the Management Report, Information on the Bank's Management and Statement of Responsibility of the Bank's Management for the financial year for which the consolidated and separate financial statements are prepared is consistent with the consolidated and separate financial statements;
- the Management Report has been prepared in accordance with the requirements of the Financial and Capital Market Commission Regulation No. 46 "Regulation on preparation of the annual report and consolidated annual report of credit institutions, investment brokerage companies and investment management companies".

In addition, in light of the knowledge and understanding of the Group and the Bank and their environment obtained in the course of the audit, we are required to report if we have identified material misstatements in the Management Report, Information on the Bank's Management and Statement of Responsibility of the Bank's Management, that we obtained prior to the date of this auditor's report. We have nothing to report in this respect.

Responsibilities of management and those charged with governance for the consolidated and separate financial statements

Management is responsible for the preparation of the consolidated and separate financial statements that give a true and fair view in accordance with 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 consolidated and separate financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated and separate financial statements, management is responsible for assessing the Group's and the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group and the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's and the Bank's financial reporting process.

Auditor's responsibilities for the audit of the consolidated and separate financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated and separate financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in

* This version of our report is a translation from the original, which was prepared in Latvian. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation.



the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated and separate financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated and separate financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Group's and the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's and the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated and separate financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group and the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the separate and consolidated financial statements, including the disclosures, and whether the separate and consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

* This version of our report is a translation from the original, which was prepared in Latvian. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation.



From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated and separate financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Consistency of the Additional Report to the Audit Committee

We confirm that our audit opinion on the consolidated and separate financial statements expressed in this report is consistent with the additional report to the Audit Committee of the Bank, which we issued on 5 July 2019 in accordance with Article 11 of the EU Regulation 537/2014.

Report on other legal and regulatory requirements

Appointment

We were appointed as auditors of the Bank and the Group by shareholders' resolution on 10 April 2019. This is the first year of our appointment as auditors.

PricewaterhouseCoopers SIA
Certified audit company
License No. 5

A handwritten signature in blue ink, appearing to read 'I. Lejiņa', is written over a light blue horizontal line.

Ilandra Lejiņa
Certified auditor in charge
Certificate No.168

Member of the Board

Riga, Latvia
5 July 2019

* This version of our report is a translation from the original, which was prepared in Latvian. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation.