MORTGAGE AND LAND BANK OF LATVIA

Condensed Consolidated and Bank Financial Statements for the year ended 31 December 2008 (unaudited)

MORTGAGE AND LAND BANK OF LATVIA
MANAGEMENT REPORT

Since 2007, global economic growth has slowed down: global economic growth in 2006 was 5.1% and 5.0% in 2007. The International Monetary Fund (IMF) estimates that the growth rate for 2008 will be 3.9% (the results are not available yet), while the growth rate for 2009 is estimated to amount to 0.5%. Two key factors have contributed to the recession of economy: unrest of the financial market (US mortgage crisis, large scale financial institution bankruptcies, loss of confidence among financial market participants, stricter credit regulations) and the growth of energy resources and food during the recent years.

The IMF estimates of the gross domestic product (GDP) growth in the European Union (EU) are 1.65% in 2008, 0.55% in 2009; in the forthcoming years, the growth will gradually increase, yet it will not achieve the pre-crisis levels in the next 5 years. In emerging countries (especially China and India) the growth of economy will continue, but it will be slower than before after the 2008-2009 recession.

The economy of Latvia has faced radical changes after the rapid growth in the previous years (11.9% in 2006, 10.2% in 2007). Economy stabilising measures (anti-inflation measures, limitation of borrowing and internal consumption) have reduced the expansion of loans, the internal consumption and the current account deficit, but the growth of gross domestic product has dropped dramatically and entered a recession. According to the estimates of the European Commission (EC), in 2008 the negative growth of Latvia's GDP will be at -2.3% in 2008, -6.9% in 2009 and -2.4% in 2010. The Bank of Latvia estimates a 2% reduction of GDP in 2008 and a 5% reduction in 2009.

The key components of the gross domestic product growth in the previous years (real estate operations, retail, construction, financial mediation) have decreased substantially and there will be no equivalent replacements for these industries during the next 2-3 years. The competitive edge of Latvian companies is seriously undermined by inflation and the increased production costs, as well as the reduced demand and the increased competition in the existing markets.

In 2008, the export of Latvia increased by 9%, while the import decreased by 4%. The export growth can be mainly attributed to metal, chemicals and food, although the growth partially consists of re-export. The reduced import and increased export led to decrease of Latvia's external trade deficit in 2008.

With the economy slowing down faster than expected, the decrease of inflation in the end of the last year exceeded expectations and in December it stood at a mere 10.5%. The reasons for the swift reduction: steep fall in demand, drop in prices of global energy resources and the subsequently reduced burden of costs. Thus, since May in last year, when the inflation reached its peak at almost 18%, it has decreased by almost a third. Taking into account the high growth of inflation in the early months of last year and the significant reduction of consumer prices in the second half of the year, the average inflation figure for 2008 resulted in 15.4%**.**

The national unemployment rate in December 2008 reached 7% (4.9% in December 2007). Since the third quarter of 2008, the characteristic line for trend, which used to point downwards, has begun going upwards. The increase is relatively small so far, because the people dismissed as a result of reduction of operations by the companies have filled the vacancies that had been protractedly unfilled or in little demand, there is a demand for seasonal workers and people do not rush to register at the unemployment registry. Although, in early 2009 the unemployment will increase more rapidly and, according to estimates of expert of the Bank, it may reach 10%. The EC estimates that the unemployment in 2010 might reach even 11.4% in Latvia.

As at December 2008, banking services in Latvia were offered by 21 banks and five branches of foreign banks. There are also seven electronic money institutions and three monetary market funds registered in the Bank of Latvia. The State Joint Stock Company Latvijas Hipotēku un zemes banka (The Mortgage and Land Bank of Latvia) is the only commercial bank that is fully state-owned. In November 2008, by a decree of the Cabinet of Ministers intended for stabilisation of Latvian financial system, the Mortgage Bank paid 2 lats and obtained 84.83% of Parex Bank shares, which means that in fact this commercial bank is also state-controlled. Considering the short-term nature of this investment and the specifics of operations related thereto, it has no substantial impact on the operations of the Mortgage Bank and it does not increase the risks undertaken by the Bank.

During 2008, the banks' assets have increased by 6% reaching 23.2 billion lats at the end of December, the amount of granted loans increased by 11%, while the deposits (with transit funds) have decreased by 4% and the equity and reserves of banks have decreased by 1%. The non-audited profit of banks in 2008 reached 77.6 million lats, which represents only 1/5 of the 2007 earnings figure.

The growth of borrowing has reduced significantly since mid-2007, which is a result of the requirements of the anti-inflation plan, rise in price of credit resources and various increased credit risks. The loan market has become more transparent, thanks to the Borrowers' Registry introduced in 2008.

The recession of Latvian economy and the increased cost of loans have affected the quality of the commercial bank credit portfolio, which has deteriorated over the last year. At the end of 2008, the percentage of loans where payments had been overdue by more than 30 days reached 8% of the total amount of the credit portfolio (1 294 million lats).

The quality of credit portfolio in the commercial banking system has mainly deteriorated in the following segments:

1) personal loans - high-price segment and speculative transactions;
2) real estate projects;
3) retail;
4) wood processing and manufacturing of furniture;
5) hotels and entertainment objects;
6) road transport.

The prospects of recovery of problematic loans are becoming more complicated, because, as the real estate market stagnates, the price of recoverable objects is falling, the realisation terms are extending and the costs are increasing. This leads to increase of the amount of written-off debts in the financial sector.

The borrowing rate in 2009 will be moderate and the banks will mainly concentrate on the quality of the granted and existing loans. New loans will be primarily granted to financing of branches and projects for promotion of export, infrastructure projects and different innovations, which can promote the competitive edge of Latvian companies.

Taking into account the rapidly decreasing growth of economy and that the slower growth of borrowing rate has reduced the role of banks in maintenance of domestic demand, the council of the Bank of Latvia reduced the reserve requirement for bank liabilities exceeding 2 years many times in 2008 (the total decrease was from 8% to 3%) and also reduced the reserve requirement for all other liabilities included in the reserve base from 8% to 5%.

Although the US Federal Reserve reduced the dollar basic interest rate several times in 2008 (the total decrease from 4.25% to 0.25%) and the European Central Bank reduced the Euro basic interest rate from 4% to 2.5%, this period saw an increase of the average interest rate for loans issued by Latvian commercial banks (except for loans to legal entities in foreign currencies). The average interest rate for private borrowers (in lats) increased from 17.3% (December 2007) to 17.5% (December 2008), while for legal entities the increase for the corresponding period was from 9.7% to 13.4%. The average interest rate for private borrowers (in foreign currencies) grew from 6.8% (December 2007) to 7.5% (December 2008), while for legal entities during the corresponding period there was a reduction from 7.2% to 13.4%.

The growth rate of the Mortgage Bank in 2008 has decreased, as the case is in the entire banking system. The gross amount of assets of the Mortgage Bank increased by 38.3 million lats or 4.1% and amounted to 962.2 million lats. By the amount of assets at the end of December, the Bank was ranked 8th among the commercial banks in Latvia (4.1% market share). The non-audited profit of the Bank for 2008 reached 1.3 million lats, which was 4.8 million lats or 79% less than for the corresponding period of the previous year. The main reason behind the reduction is formation of reserves for insecure assets.

The credit portfolio of the Mortgage Bank increased by 69 million lats or 10.4% in 2008 and amounted to 731.6 million lats. The bank was ranked 6th among Latvian commercial bank according to the size of its credit portfolio (4.4% market share). The Mortgage Bank was the seventh largest bank in Latvia by the amount of loans issued to businesses (5.2% market share) and the seventh largest bank by the amount of loans issued to private borrowers (3.3% market share).

The amount of deposits in the Bank during 2008 increased by 19 million lats or 7% and amounted to 298 million lats. The Mortgage Bank was ranked 10th among Latvian commercial banks by the amount of deposits (including transit funds) at the end of December (3.1% market share).

The amount of debt securities issued by the Mortgage Bank decreased by 11.4 million lats or 21% in 2008 and amounted to 42 million lats. In May, the Bank issued mortgage bonds worth EUR 12.7 million; in June, bonds worth LVL 10 million and EUR 9 million were retired, which were the first short-term bonds in the Baltic States listed on the stock exchange and not issued by the State Treasury.

To provide the customers with an opportunity to conveniently place their funds and make savings in pension funds, in the first half of 2008, the Mortgage Bank completed the acquisition process of IPS Suprema Fondi and formed a Joint Stock Company Ieguldījumu pārvaldes sabiedrība HIPO FONDI (Investment Management Company HIPO FONDI), and also commenced the attraction of customers to three second-level pension plans in all three Baltic branches.

During the second half of 2008 and in early 2009, the international credit rating agencies have gradually decreased their ratings for Latvia to the lowest investment grade, pointing out that the downgrading of credit ratings reflects the recession of the economic situation, which has been sharper that predicted. The Mortgage Bank is a fully state-owned bank and its rating cannot exceed that of the country.

Thus, the *Moody's Investor service* international agency downgraded the rating of the Mortgage Bank along with that of Latvia. The ratings for the bank are as follows:

- long-term foreign currency investments – ***Baa1*** (future outlook - negative),
- short-term foreign currency investments – ***P2***,
- financial stability rating – ***D-*** (future outlook - negative),
- mortgage bond rating – ***A2***,

which are investment grade ratings.

In 2008, the Mortgage Bank continued to implement various development programmes, which, by assignment of the government, include providing support to certain groups of businesses and individuals - crediting programmes for small and medium enterprises, housing guarantee programme, rural development programme. The Banks, as a national bank, pays particular attention to implementation of programs that can help Latvian businessmen continue or commence their business even in such adverse economic conditions.

2008 saw the completion of the programme co-financed by the European Social Fund - Training, Consulting and Financial Support for Commencement of Business and Self-Employment. The project included training of 998 future businessmen, 600 applicants for the support submitted their business plans and 327 of them were granted financial support in the form of grants and loans.

2008 also saw the completion of the programme co-financed by the European Regional Development Fund - Crediting of Beginners in Business. 291 loans totalling at 22.76 million lats were granted under this project.

To promote business activity in Latvia, the Cabinet of Ministers issued a decree on the 22nd of May 2008 (decree No. 275) to commence a new programme - Support Programme for Improvement of Competitiveness of Businesses, which would be implemented by the Mortgage Bank. Until the end of the year, there were 32 loans granted for the total amount of 14.17 million Euros under this programme.

In August, the Mortgage Bank commenced cooperation with the association *Support Fund for Latvian Businesswomen in Rural Areas* concerning the support of business organised by women in rural areas in Latvia, which provides micro-loans for development of business. The 50 000 lats provided for the project have been acquired.

During 2008, the Mortgage Bank and environment protection activist groups have jointly implemented several projects the invite the society to act in an environmentally friendly way and to think in long term. Some of the examples include: the Green Guidebook devoted to green way of living published and promoted together with the organisation Zaļā Brīvība (Green Freedom) and the project of preservation of sand-dunes carried out jointly with the Green Movement of Latvia. In this way the Mortgage Bank presents itself as a socially responsible entity.

The Mortgage Bank continued cooperation with the Platforma Records record company and issued CDs with fairy-tales for children and their parents. Four records were issued in total: Grimm's Fairy Tales, Emil and the Berlin Boys, Peter Pan, and the Cat's Mill. This project demonstrates that the family is one of the most important values for the Bank.

In the second quarter of 2008, the Mortgage Bank and Aizkraukles Bank concluded an agreement on financing of small and medium enterprises, whereby the Mortgage Bank provides the Aizkraukles Bank with a syndicated loan worth 10 million Euros required for the implementation of the programme.

Early in the year, the Bank signed cooperation agreements with leaders of all regional funds in Latvia, as well as with the Limbaži Region Council on organisation or project tenders. The Mortgage Bank supported the best works of project tenders staged by the funds, which promote the self-initiative of local residents for improvement of their living environment.

Early 2008 saw the commencement of a large-scale education programme for residents and building managers on the renovation of residential buildings - from regional seminars, informative articles in the press, expert opinions, informative video clips and handouts, to participation in projects organised by other institutions. In 2008, 100 loans for renovation of residential buildings were granted, which amounted to 2.5 million lats in total.

The quality of Bank services has been appreciated by customers. In March, the offices of the Mortgage Bank participated in the event called Praise Good Service organised by *Labsserviss.lv*, which included participation from 50 Latvian companies with 800 service points, and the Rēzekne office of the Mortgage Bank was placed among top 10 in this competition.

One of the priorities of the Mortgage Bank in 2008 has been the financing of innovation projects. Active work was directed towards the achievement of this goal, and, as a result, 10% of all loans granted in 2008 have been destined for implementation of innovations in businesses.

In 2008, the Mortgage Bank continued to update and improve the network of offices and sub-branches. The Balvi office started work in brand-new premises in January, followed by a sub-branch of the Riga office in June, which is located in Riga, in the premises of Land Register Department. The Ūnijas office also has moved to new, larger premises in October. In order to optimise the Bank operations, the Salacgrīva sub-branch was closed in March 2008. As at the end of 2008, the Bank is located in 29 offices in Riga and in each regional centre of Latvia, as well as 8 sub-branches in different regions of Latvia.

17 new ATMs were installed during 2008: in the newly opened Balvi office, Ādaži, Ezere, Jūrkalne, Piltene, Dobele, Cesvaine, Barkava, Riga (in the premises of the sub-branch of the Riga office), Lēdmane, Rēzekne, Krāslava, Pļaviņas, Rugāji, Nītaure, Skaistkalne and Lejasciems. Thus, the network of ATMs of the Mortgage Bank consisted of 58 ATMs at the end of 2008. In September 2008, the Mortgage Bank concluded an agreement with the SEB Banka on a *friendly* ATM network - as from the 1st October, the customers of the Mortgage Bank can withdraw cash free of charge from 58 ATMs of the Mortgage Bank, 14 ATMs of the Rietumu Banka, 202 ATMs of Latvijas Krājbanka and, in addition, 218 ATMs of the SEB Banka throughout Latvia. At the end of 2008, the network of ATMs of the Mortgage Bank and the *friendly* ATM network accounted for almost a half of the total network of ATMs in Latvia.

In the fourth quarter of 2008, the Information Technology Department of the Bank successfully completed the transition of the ATM network from the network of First Data Latvia (FDL) to the Bank's management network, thus improving the functionality and the options of monitoring of the ATMs.

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

Supervisory Council (at 31 December 2008)

Baiba Bāne	Chairman of the Council
Dāvids Tauriņš	Deputy Chairman of the Council (appointed on 1 November 2008)
Jānis Šnore	Member of the Council
Matīss Markuss	Member of the Council (appointed on 1 November 2008)
Iveta Strautiņa	Member of the Council

During the reporting period, the following Council members resigned: Ms. Gundega Šulca, Mr. Andris Liepiņš, Ms. Vija Gēme, Ms. Dace Ratniece and Ms. Baiba Paševica.
Mr. Dāvis Tauriņš and Mr. Matīss Markuss were appointed as Council members.

Board of Directors (at 31 December 2008)

Inesis Feiferis	Chairman of the Board
Rolands Paņko	Deputy Chairman of the Board
Aija Laicāne	Member of the Board
Jēkabs Krieviņš	Member of the Board
Andris Riekstiņš	Member of the Board

STATEMENT OF RESPONSIBILITY OF THE MANAGEMENT

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

Management confirms that suitable accounting policies have been used and applied consistently and reasonable and prudent judgments and estimates have been made in the preparation of the condensed consolidated and bank financial statements for the period ended 31 December 2008. Management also confirms that applicable International Financial Reporting Standards as adopted in EU have been used in preparation of the financial statements and that these financial statements have been prepared on a going concern basis. Appropriate accounting policies have been applied on a consistent basis.

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

INCOME STATEMENT
(all amounts in thousands of Euro)

	2008		2007	
	Group	**Bank**	**Group**	**Bank**
Interest income	94,061	90,418	74,626	71,107
Interest expense	(63,937)	(62,698)	(42,883)	(42,631)
Net interest income	**30,124**	**27,720**	**31,743**	**28,476**
Fee and commission income	5,821	5,700	5,851	5,838
Fee and commission expense	(1,419)	(1,383)	(1,315)	(1,224)
Net fee and commission income	**4,402**	**4,317**	**4,536**	**4,614**
Dividend income	18	1,157	-	711
Net trading income	3,068	3,108	3,048	3,004
Other operating income	6,783	4,895	5,986	4,452
Staff costs	(14,368)	(12,799)	(14,280)	(12,942)
Administrative expenses	(13,021)	(11,545)	(11,981)	(10,903)
Depreciation and amortisation	(3,325)	(2,877)	(3,510)	(3,270)
Provision for impairment losses	(13,204)	(12,159)	(4,589)	(4,055)
Profit before income tax	**477**	**1,817**	**10,953**	**10,087**
Income tax expense	(219)	(100)	(1,683)	(1,342)
Net profit for the period	**258**	**1,717**	**9,270**	**8,745**
Attributable to:				
Equity holders of the Bank	255	-	-	-
Minority interest	3	-	-	-

BALANCE SHEET
(all amounts in thousands of Euro)

	31/12/08		31/12/07	
Assets	**Group**	**Bank**	**Group**	**Bank**
Cash and balances with Central Bank	64,193	64,193	94,287	94,287
Trading securities	5,491	5,280	4,651	4,651
Investment securities – held to maturity	91,163	91,020	18,583	18,583
Investment securities – available for sale	37,416	37,416	77,021	77,021
Due from credit institutions	93,322	92,962	149,218	148,921
Derivative financial instruments	2,250	2,250	120	120
Loans to customers	1,056,320	1,033,823	950,276	939,593
Investment properties	2,598	2,598	3,011	3,011
Investments in subsidiaries and associated undertakings	421	1,278	785	1,312
Intangible assets	3,463	2,763	2,871	2,742
Property and equipment	12,389	10,868	12,770	11,307
Current income tax assets	1,632	1,429	455	404
Other assets	7,114	2,071	4,640	1,026
Deferred expenses and accrued income	1,022	802	1,154	980
Total assets	**1,378,794**	**1,348,753**	**1,319,842**	**1,303,958**
Liabilities				
Due to credit institutions	733,103	705,641	707,597	695,412
Due to customers	429,847	430,005	401,426	402,032
Derivative financial instruments	777	777	185	185
Transit funds	3,238	3,238	3,664	3,664
Issued debt securities	57,854	57,854	74,692	74,692
Other liabilities	18,616	17,613	17,023	15,952
Deferred income and accrued expenses	3,714	2,678	3,968	2,962
Current income tax liabilities	-	-	70	-
Deferred tax liabilities	1,431	1,431	1,370	1,332
Subordinated liabilities	44,236	44,236	18,927	18,927
Total liabilities	**1,292,816**	**1,263,473**	**1,228,922**	**1,215,158**
Shareholder's equity				
Share capital	69,028	69,028	69,028	69,028
Reserve capital	3,591	2,935	3,591	2,935
Minority interest	41	-	-	-
Revaluation deficit on available for sale investments	(5,068)	(5,068)	(2,191)	(2,191)
Retained earnings	18,386	18,385	20,492	19,028
Total shareholder's equity	**85,978**	**85,280**	**90,920**	**88,800**
Total liabilities and shareholder's equity	**1,378,794**	**1,348,753**	**1,319,842**	**1,303,958**
Off balance sheet items				
Contingent liabilities	34,159	34,159	16,300	16,300
Financial commitments	42,325	56,060	60,465	94,087

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

	Attributable to equity holders					
	Share Capital	**Reserve capital**	**Revaluation deficit on available for sale investments**	**Retained earnings**	**Minority interest**	**Total equity**
Balance as at 31 December 2006	**69,028**	**3,591**	**(875)**	**13,214**	**-**	**84,958**
Distribution of profit – payment for use of state capital	-	-	-	(1,992)	-	**(1,992)**
Net loss on available for sale investments	-	-	(1,316)	-	-	**(1,316)**
Profit for the period	-	-	-	9,270	-	**9,270**
Balance as at 31 December 2007	**69,028**	**3,591**	**(2,191)**	**20,492**	**-**	**90,920**
Distribution of profit – payment for use of state capital	-	-	-	(2,361)	-	**(2,361)**
Net loss on available for sale investments	-	-	(2,877)	-	-	**(2,877)**
Minority share of IPAS „Hipo fondi" on the date of acquisition*	-	-	-	-	38	**38**
Profit for the period	-	-	-	255	3	**258**
Balance as at 31 December 2008	**69,028**	**3,591**	**(5,068)**	**18,386**	**41**	**85,978**

* IPAS "Hipo fondi" was acquired in February 2008 and the Group owns 83% of IPAS "Hipo fondi" shares.

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

	Share Capital	**Reserve capital**	**Revaluation deficit on available for sale investments**	**Retained earnings**	**Total equity**
Balance as at 31 December 2006	**69,028**	**2,935**	**(875)**	**12,275**	**83,363**
Distribution of profit – payment for use of state capital	-	-	-	(1,992)	**(1,992)**
Net loss on available for sale investments	-	-	(1,316)	-	**(1,316)**
Profit for the period	-	-	-	8,745	**8,745**
Balance as at 31 December 2007	**69,028**	**2,935**	**(2,191)**	**19,028**	**88,800**
Distribution of profit – payment for use of state capital	-	-	-	(2,361)	**(2,361)**
Net loss on available for sale investments	-	-	(2,877)	-	**(2,877)**
Profit for the period	-	-	-	1,717	**1,717**
Balance as at 31 December 2008	**69,028**	**2,935**	**(5,068)**	**18,384**	**85,279**

CASH FLOW STATEMENT
(all amounts in thousands of Euro)

	2008		2007	
	Group	**Bank**	**Group**	**Bank**
Cash flows from operating activities				
Profit before taxation	477	1,817	10,953	10,087
Depreciation and amortisation	3,325	2,877	3,510	3,270
Increase in provision for impairment losses	10,309	9,506	2,063	1,559
(Profit) / loss from foreign exchange revaluation	-	-	3	47
Profit from sale of property and equipment	(139)	(1)	(7)	(11)
Increase in deferred income and accrued expenses	997	745	1,841	1,480
(Increase) / decrease in deferred expenses and accrued income	132	178	(293)	(252)
Increase in other assets	(8,401)	(6,669)	(2,511)	(1,872)
Increase / (decrease) in other liabilities	2,186	2,254	9,836	9,557
Increase in cash and cash equivalents from operating activities before changes in assets and liabilities	**8,886**	**10,707**	**25,395**	**23,865**
Increase in balances due from credit institutions	(13,261)	(13,261)	(21,413)	(21,413)
Increase in loans to customers	(113,520)	(101,089)	(241,577)	(244,952)
Decrease in trading securities	(840)	(629)	(566)	(566)
Increase in balances due to credit institutions	18,782	3,783	268,919	272,090
Increase / (decrease) in balances due to customers	28,420	27,972	11,498	11,902
Decrease in transit funds	(425)	(425)	(418)	(418)
Increase / (decrease) in debt securities issued	(16,838)	(16,838)	13,209	13,209
Cash and cash equivalents generated from / (used in) operating activities	**(88,796)**	**(89,780)**	**55,047**	**53,717**
Corporate income tax paid	**(1,476)**	**(1,026)**	**(3,056)**	**(2,489)**
Cash flows from investing activities				
Increase in investment securities	(35,616)	(35,474)	(24,213)	(24,213)
Purchases of property and equipment	(3,914)	(2,517)	(5,787)	(4,402)
Proceeds from property and equipment disposal	518	60	85	23
Proceeds from investments in associated entities disposal	386	34	28	3
Acquisition of investments in associated entities	(21)	-	(213)	(712)
Cash and cash equivalents used in investing activities	**(38,647)**	**(37,897)**	**(30,100)**	**(29,301)**
Cash flows from financing activities				
Proceeds from subordinated debt	25,304	25,304	-	-
Dividend paid	(2,360)	(2,360)	(1,992)	(1,992)
Cash and cash equivalents generated from / (used in) financing activities	**22,944**	**22,944**	**(1,992)**	**(1,992)**
Increase / (decrease) in cash and cash equivalents	(105,975)	(105,759)	19,899	19,935
Cash and cash equivalents at the beginning of the period	187,728	187,615	167,832	167,728
Effect of exchange rates on cash and cash equivalents	-	-	(3)	(47)
Cash and cash equivalents at the end of the period	**81,753**	**81,856**	**187,728**	**187,616**

GENERAL INFORMATION

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

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

RISK MANAGEMENT

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

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

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

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

Credit Risk

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

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

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

The Bank's Risk Management Committee monitors the credit risk, including credit risk concentrations, and the quality of the credit portfolio, whereas central, regional and branch credit committees are taking decisions on the credit risk within the approved limits.

RISK MANAGEMENT (continued)

The Bank's Risk Management Department is responsible for analysis of the credit risk concentration, setting and controlling the limits as well as the evaluation of the quality of the credit portfolio, whereas the Bank's Loan Department and Treasury Department is responsible for daily credit risk management in lending operations and operations with financial instruments respectively.

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

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

– ratio of large exposure concentration and own funds (internal limit - 400%, limit set by the Law on Credit Institutions – 800%), as of 31.12.2008.. was 78.6% (as of 31.12.2007.-79%);
– ratio of single client's (related clients' group) large exposure and own funds, which can not exceed 25%, as of 31.12.2008. was 22.1% (as of 31.12.2007.-16.6%);
– proportion of risk concentration in single economic sector in the Bank's credit portfolio and own funds as of 31.12.2008. was 172.6% (as of 31.12.2007.-195.9%);
– ratio of risk exposures with persons related to the Bank and own funds, which can not exceed 15%, as of 31.12.2008. was 3.8% (as of 31.12.2007.-6.1%).

Since the Bank's strategy is not focused on servicing the non-residents business, the proportion of the Bank's total claims to non-residents was small and as of 31.12.2008. was 8.9% (as 31.12.2007.–7.7%) of the Bank's total assets. The Group and the Bank manages the country risk that results from the lending operations to non-residents according to the Country Risk Management Policy.

Liquidity Risk

The liquidity risk relates to the ability of the Group and the Bank to redeem the legally valid claims of its customers and other creditors in due time and secure that the increase of the anticipated claims presents reasonable costs. The Liquidity Risk Management Policy of the Bank stipulates the principles for management of liquidity risk. The Bank shall ensure that the liquid assets are not less than 30% (set by the FCMC) of its short-term liabilities at all times. The Assets and Liabilities Committee of the Bank stipulates the guidelines for liquidity risk management and controls compliance thereof, whereas the Treasury Department provides for daily management of the liquidity risk. To evaluate the liquidity risk, the Bank uses the GAP method. The Bank has set liquidity net position limit in each significant currency and total liquidity net position limit as well as maximum deposit amount from a single depositor to control the liquidity risk. Liquidity ratio (min – 30%) as of 31.12.2008. was 60.4% (as of 31.12.2007.-99.4%).

Foreign Currency Risk

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

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

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

Interest Rate Risk

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

The Assets and Liabilities Management Committee monitors the interest rate risk, whereas the Treasury Department is responsible for the daily management of the interest rate risk.

RISK MANAGEMENT (continued)

The Bank has set limit on changes in economic value of the Bank at 10% of own funds and limit on changes in net interest income at 2% of own funds which as of 31.12.2008. were 9.76% (as of 31.12.2007.-7.96%) and 0.27% (as of 31.12.2007.-0.93%) respectively.

Operational risk

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

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

Capital Adequacy

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

As at 31 December 2008 the capital adequacy ratio of the Bank calculated according to the regulations of the Financial and Capital Market Commission were 9.6% (as of 31.12.2007.-9.9%) which exceeded the minimum of 8%.

THE PERFORMANCE RATIOS OF THE BANK

Items	Accounting period	Previous accounting year
Return on equity (ROE) (%)	1.93%	10.58%
Return on assets (ROA) (%)	0.14%	0.78%

CONSOLIDATION GROUP

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

* IPS – investment management company, CFI – other financial institution, CKS – other commercial company.
** MS – subsidiary; KS – joint venture.

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

Rating type	Ratings	Rating Approval date	Previous rating
For long-term foreign currency bank deposits	**Baa1**	10.07.2008.	**A3**
For short-term foreign currency deposits	**P2**	10.07.2008.	**P2**
The financial strength rating	**D-**	10.07.2008.	**D-**
The rating of mortgage bonds issued	**A2**	10.07.2008.	**A1**

Moody`s Investors Service reports of the Bank may be found at: *www.hipo.lv*
Additional information on the ratings assigned (incl. Legend of ratings) may be found at: *www.moodys.com*

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

Inesis Feiferis
Chairman of the Board

Uvis Zemītis
Chief Accountant