Annual report
for year 2018

Expobank

CONTENTS

REPORT OF THE BOARD OF DIRECTORS AND THE MANAGEMENT BOARD

Dear customers and business partners,

Compared to the previous years, Latvia's economic development in 2018 became more robust – one of the fastest growing economies within the European Union (EU). It is anticipated that the total aggregate Gross Domestic Product (GDP) in 2018 increased by at least 4,7% which is more than in year 2017. Exports, investments and private consumption is expanding at a steady rate. Considering the economic growth inside the EU countries and the availability of investments from the EU funds, it is expected that a stable economic growth will continue its course into the year 2019 as well.

Latvia has been a member country of the "eurozone" for the past five years and some of the most significant and positive gains from the conversion to the Euro currency have been: an increase of Latvia's credit ratings and the country's further integration into the EU. The adoption and implementation of the Euro currency in Latvia created the conditions which ensured that the inflation level during these years has remained low, and the overall average annual inflation rate for the year 2018 could be projected at level of 2,6%.

Latvia's economic stability also has been reaffirmed by credit ratings assigned by international credit rating agencies. In 2018, Fitch (A-) and Moody's (A3) agencies maintained the previously assigned credit rating in the investment grade category, however, Standard & Poor's has increased its rating to level "A", subsequently augmenting a more favorable investments environment and better borrowing options for private borrowers as well as the country as a whole.

A study done by the World Bank (Doing Business 2018) shows the ranking of countries in terms of the "business-friendly" environment (ease of doing business), and Latvia's targeted reforms and close collaboration with the private sector in 2018 made it possible to retain the high 19th place out of a global competition of 190 countries.

The only sector that posted a drop during 2017-2018 was the financial sector, which to a large extent was driven by the regulatory changes in the banking/financial sector and the resultant reduction in servicing of non-resident customers.

Over the last 27 years, AS Expobank (hereinafter - the Bank), being one of the oldest financial institutions in Latvia, has also been one of the most financially stable banks in Latvia, maintaining high capital adequacy and liquidity during periods of vigorous growth as well as periods of change and instability.

The Banks efforts focus on mitigating risks inherent to servicing the business needs of international customers in an environment of tightening regulatory requirements, continuing reforms of the financial markets, increasing geopolitical and reputational risks, as well as the changes in correspondent banking with US-based banks. In response to these new challenges, the Banks management in 2018 approved the new Business Strategy for 2018-2020, which changes the business model by further diversifying the customer base and refocusing its operations primarily towards servicing companies and private individuals in Latvia, the Baltic countries and other EU countries, with the aim of forming a more sustainable customer base in the long run.

The Bank continues to follow a stable and conservative risk management policy. The Bank utilizes precautionary measures in its daily operations, assuming risk only for business activities of customers that are well known to the Bank, prevents the likelihood of excessive risk in any business dealings of its customers, and restricts or refuses to carry out a transaction if a possibility of an increased risk is identified.

In 2018, the Bank implemented a variety of risk-mitigating measures in the areas of money laundering and terrorism financing (hereinafter - AML/CFT) to safeguard a moderate risk level at the Bank. An international audit firm completed an independent review of AML/CFT risk management at the Bank and the performance evaluation of internal control system and information technology and solutions - tools which ensure the functionality of AML/CFT risk control at the Bank. A concluding report was submitted by the auditors to the management of the Bank and the recommendations outlined in the report will be implemented in 2019.

For the 2018 financial year the Bank's net profit was EUR 318 thousand. The Bank's top priority remains the operational stability, supported by the Bank's capital adequacy ratio of 73,0% (compared to the minimum OCR (overall capital requirement) ratio of 14,1%, set by the regulator), high liquidity ratio of 185,2% (vs. required 60%) as well as liquidity coverage ratio (LCR) of 898% (vs. required 100%).

The average number of employees at the Bank in 2018 was 65. Furthermore, at the end of 2018, the Bank had made a decision to close its branch in the Republic of Cyprus.

REPORT OF THE BOARD OF DIRECTORS AND THE MANAGEMENT BOARD

During 2019, the Bank will continue to put into practice its mission to be a responsible and professional member of the financial sector observing these values in its daily operations and in conducting business with its clients, fellow colleagues, and the society in general. The Bank will continue to pay close attention to ensuring the safety of information and data protection while investing additional resources in information systems and technologies.

We would like to extend our utmost gratitude to all of our customers and business partners for their long-standing trust and loyalty, as well as to all of our employees for their input towards the provision of stability at the Bank and enhancing the Bank's further development.

Chairman of the Board of Directors
Ilya Mitelman

Chairman of the Management Board
Gints Čakāns

6 March 2019

MEMBERS OF THE BOARD OF DIRECTORS AND THE MANAGEMENT BOARD

As at 31 December 2018, the Members of the Board of Directors of the Bank were as follows:		
Name	**Position**	**Date of first election**
Ilya Mitelman	Chairman of the Board of Directors	01/11/2017
Kirill Nifontov	Deputy Chairman of the Board of Directors	09/02/2012
Igor Kim	Member of the Board of Directors	09/02/2012
Ingrīda Blūma	Member of the Board of Directors	01/11/2014

In 2018, there were no changes in the compostion of the Board of Directors (in 2017, all the above mentioned members of the Board of Directors were re-elected to the composition of the Board of Directors).

As at 31 December 2018, the Members of the Management Board of the Bank were as follows:		
Name	**Position**	**Date of first election**
Gints Čakāns	Chairman of the Management Board	01/09/2011
Evija Sloka	Deputy Chairperson of the Management Board	02/11/2012
Rolands Legzdiņš	Member of the Management Board	05/04/2017

On 1 November 2018, the Bank's Board of Directors re-elected Gints Čakāns and Evija Sloka to the composition of the Management Board and once again appointed Gints Čakāns as the Chairman of the Management Board and Evija Sloka as the Deputy Chairperson of the Management Board.

STATEMENT OF MANAGEMENT'S RESPONSIBILITY

Management of AS Expobank is responsible for the preparation of the financial statements of the Bank. The financial statements have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union, and comply with legislative requirements of the Republic of Latvia.

The financial statements on pages 13 to 73 are prepared in accordance with source data and present fairly the financial position of the Bank as at 31 December 2018 and the results of operations and cash flows of the Bank for the year ended 31 December 2018.

The aforementioned financial statements are prepared on a going concern basis, consistently applying accounting policies in conformity with International Financial Reporting Standards as adopted by the European Union, and relevant legislation of the Republic of Latvia. Prudent and reasonable judgments and estimates have been made by the management in the preparation of the financial statements.

The management of AS Expobank is responsible for maintenance of proper accounting system, safeguarding of the Bank's assets, and prevention and detection of fraud and other irregularities. The management is also responsible for operating the Bank in compliance with the Law on Credit Institutions, regulations of the Financial and Capital Market Commission of the Republic of Latvia, Bank of Latvia, and other laws of the Republic of Latvia applicable to credit institutions.

On behalf of the Bank's management,

Chairman of the Management Board Gints Čakāns	Deputy Chairperson of the Management Board Evija Sloka	Member of the Management Board Rolands Legzdiņš

6 March 2019

Translation from Latvian original*

INDEPENDENT AUDITOR'S REPORT

To the shareholder of AS Expobank

Report on the Audit of the financial statement

Our opinion

In our opinion, the financial statements of AS Expobank (the "Bank") set out on pages 13 to 73 of the accompanying annual report, give a true and fair view of the financial position of the Bank as at 31 December 2018, and of the financial performance and the cash flows of the Bank for the year then ended in accordance with the International Financial Reporting Standards as adopted by the European Union (IFRSs).

Our opinion is consistent with our additional report to the Audit Committee.

What we have audited

The Bank's financial statements comprise:

- the statement of financial position as at 31 December 2018;
- the statement of comprehensive income for the year then ended;
- the statement of cash flows for the year then ended;
- the statement of changes in shareholder's equity for the year then ended; and
- the notes to the financial statements, which include a summary of 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 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

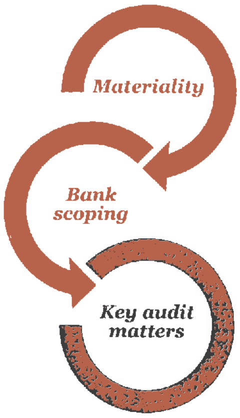
We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code) and the ethical requirements of the Law on Audit Services that are relevant to our audit of the financial statements in the Republic of Latvia. We have fulfilled our other ethical responsibilities in accordance with the IESBA Code and the ethical requirements of the Law on Audit Services.

To the best of our knowledge and belief, we declare that non-audit services that we have provided to the Bank and its related entities are in accordance with the applicable law and regulations in Latvia and that we have not provided non-audit services that are prohibited under Article 37.6 of Law on Audit Services of the Republic of Latvia.

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

Our audit approach

Overview



Overall Bank materiality is 222 thousand EUR, which represents approximately 0.6% of net assets.

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

Fee and commission income.

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in 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. As in all of our audits, 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 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 Bank materiality for the 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 Bank materiality	Overall materiality applied to the Bank was EUR 222 thousand.
How we determined it	0.6% of net assets of the Bank.
Rationale for the materiality benchmark applied	We chose net assets as the base benchmark because, in our view, it is the benchmark which is of primary focus by the users of the financial statements and forms the

* 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.

	basis for capital adequacy for regulatory purposes. We chose 0.6%, which is within the range of acceptable quantitative materiality thresholds for this benchmark.

We agreed with the Audit Committee that we would report to them the misstatements identified during our audit above EUR 11 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.

Key audit matter	*How our audit addressed the key audit matter*
Fee and commission income Refer to Note 6 '*Fee and commission income*' of the financial statements. Fee and commission income is the main source of external revenue for the Bank, therefore verification of the occurrence and accuracy of fee and commission income was the main focus area of our audit. Although the commissions are based on the approved price lists, transactions also include some level of manual input.	We assessed whether the accounting policies of the Bank in relation to the fee and commission income are in compliance with IFRSs. We selected a sample of the transactions and verified that the commission fee was correctly applied based on the approved price list or the agreement with the customer. We also verified supporting documents to confirm the occurrence of the transaction or event which is subject to commission fee and that the commission was recorded in the correct service period. We found no material misstatements from our testing. We verified the disclosures in the financial statements in respect of fee and commission income and found them appropriate.

Reporting on other information including the Report of the Board of Directors and the Management Board

Management is responsible for the other information. The other information comprises the Report of the Board of Directors and the Management Board, the list of Members of the Board of Directors and the Management Board, and Statement of Management's Responsibility, as set out on pages 3 to 6 of the accompanying Annual Report, which we obtained prior to the date of this auditor's report.

Our opinion on financial statements does not cover the other information, including the Report of Directors and the Management Board, Members of Directors and the Management Board, and Statement of Management's Responsibility.

In connection with our audit of the 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 financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

With respect to the Report of the Board of Directors and the Management Board, we also performed the procedures required by Law on Audit Services. Those procedures include considering whether the 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 Report of the Board of Directors and the Management Board, Members of the Board of Directors and the Management Board, and the Statement of Management's Responsibility for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Report of the Board of Directors and the Management Board 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 of credit institutions, investment brokerage companies and investment management companies".

In addition, in light of the knowledge and understanding of 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 Report of the Board of Directors and the Management Board Members of the Board of Directors and the Management Board, and the Statement of Management's Responsibility, 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 financial statements

Management is responsible for the preparation of the 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 financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing 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 Bank or to cease operations, or has no realistic alternative but to do so.

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

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the 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 the aggregate, they could reasonably be expected to

* 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.

influence the economic decisions of users taken on the basis of these 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 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 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 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 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 Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the 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.

Report on other legal and regulatory requirements

Appointment

We were first appointed as auditors of the Bank on 6 October 2016. Our appointment has been renewed by shareholder resolution on 1 November 2018 representing a total period of uninterrupted engagement appointment of 3 years.

PricewaterhouseCoopers SIA
Certified audit company
License No. 5

Ilandra Lejiņa
Certified auditor in charge
Certificate No.168

Member of the Board

Riga, Latvia
6 March 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.

STATEMENT OF COMPREHENSIVE INCOME

	Note	2018 EUR'000	2017 EUR'000
Continuing operations			
Interest income	5	1,102	3,291
Interest expense	5	(400)	(857)
Net interest income		**702**	**2,434**
Fee and commission income	6	4,161	5,740
Fee and commission expense	7	(164)	(359)
Net fee and commission income		**3,997**	**5,381**
Net income from transactions with financial instruments	8	930	2,836
Other income		348	636
Other expenses	9	(1,134)	(1,375)
Impairment or reversal of impairment on financial assets		5	-
General administrative expenses	10	(4,502)	(6,093)
Profit before income tax		**346**	**3,819**
Income tax expense	11	(28)	(345)
Profit from continuing operations		**318**	**3,474**
Losses from sale of subsidiaries	21	-	(6,903)
Profit/(losses) for the year		**318**	**(3,429)**
Items that may be reclassified subsequently to profit or loss			
Net gains on investments in available for sale assets		NA	(207)
Net gains on investments in available for sale assets reclassified to profit or loss on disposal		NA	(247)
Net gains on financial assets measured at FVOCI		(151)	NA
Net loss on financial assets measured at FVOCI reclassified to profit or loss on disposal		(25)	NA
Other comprehensive (expenses) for the year		**(176)**	**(454)**
Total comprehensive income/(expenses) for the year		**142**	**(3,883)**

The accompanying notes on pages 17 to 73 form an integral part of these financial statements.
The financial statements as set out on pages 13 to 73 were approved for issue by the Management Board on 6 March 2019.

Chairman of the Management Board Gints Čakāns	Deputy Chairperson of the Management Board Evija Sloka	Member of the Management Board Rolands Legzdiņš

STATEMENT OF FINANCIAL POSITION

	Note	31.12.2018 EUR'000	31.12.2017 EUR'000
ASSETS			
Cash and demand deposits with the central banks	12	13,566	73,724
Due from financial institutions	14	33,198	122,620
Loans and advances due from customers	15	4	8
Financial assets measured at fair value through other comprehensive income (2017: Available for sale)	16	33,667	28,223
Property and equipment	17	381	502
Intangible assets	18	343	446
Overpaid current income tax		452	269
Other assets	19	639	1,461
Total Assets		**82,250**	**227,253**
LIABILITIES AND SHAREHOLDER'S EQUITY			
Deposits and balances due to financial institutions	20	1	3,191
Current accounts and deposits due to customers	22	44,631	186,321
Accrued liabilities	23	110	97
Deferred income		-	68
Other tax payable		4	88
Other liabilities	24	516	634
Total Liabilities		**45,262**	**190,399**
Share capital		11,644	11,644
Share premium		6,360	6,360
Revaluation reserve		40	216
Other reserves		25	25
Retained earnings		18,919	18,609
Total Shareholder's Equity	**25**	**36,988**	**36,854**
Total Liabilities and Shareholder's Equity		**82,250**	**227,253**
Contingent liabilities and commitments	26	49	207
Funds under trust management	**28**	**74,149**	**120,913**

The accompanying notes on pages 17 to 73 form an integral part of these financial statements.
The financial statements as set out on pages 13 to 73 were approved for issue by the Management Board on 6 March 2019.

Chairman of the Management Board Gints Čakāns	Deputy Chairperson of the Management Board Evija Sloka	Member of the Management Board Rolands Legzdiņš

6 March 2019

STATEMENT OF CASH FLOWS

	2018 EUR'000	2017 EUR'000
CASH FLOWS FROM OPERATING ACTIVITIES		
Profit/ (loss) before income tax	346	(3,084)
Amortisation and depreciation	332	415
Interest income	(1,102)	(3,291)
Interest expense	400	857
Disposal of fixed assets	64	184
Loss from disposal of subsidiaries	-	6,903
Net increase/(decrease) in provisions	5	(360)
Increase in cash and cash equivalents before changes in assets and liabilities, as a result of ordinary operations	**45**	**(1,624)**
Decrease in available for sale assets	-	6,888
Increase in financial assets measured at fair value through other comprehensive income	(5,303)	-
Decrease/ (increase) in due from financial institutions	5	(5)
Decrease in loans	4	10,763
Decrease in other assets	822	1,517
Decrease in current accounts and deposits due to customers	(141,697)	(43,788)
Decrease in other liabilities	(268)	(2,720)
Decrease in cash and cash equivalents from operating activities before corporate income tax	**(146,392)**	**(25,721)**
Interest received	780	5,011
Interest paid	(393)	(865)
Corporate income tax (paid)/recovered	(211)	211
Net cash and cash equivalents from operating activities	**(146,216)**	**(21,364)**
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property and equipment and intangible assets	(172)	(300)
Investment in subsidiary	-	(745)
Decrease in cash and cash equivalents from investing activities	**(172)**	**(1,043)**
CASH FLOWS FROM FINANCING ACTIVITIES		
Dividends paid	-	(20,000)
Decrease in cash and cash equivalents from financing activities	**-**	**(20,000)**
Net cash flows for the period	**(146,388)**	**(42,409)**
Cash and cash equivalents at the beginning of the year	**193,153**	**235,559**
Cash and cash equivalents at the end of the year	**46,765**	**193,153**

The accompanying notes on pages 17 to 73 form an integral part of these financial statements.The financial statements as set out on pages 13 to 73 were approved for issue by the Management Board on 6 March 2019.

Chairman of the
Management Board
Gints Čakāns
6 March 2019

Deputy Chairperson of the
Management Board
Evija Sloka

Member of the
Management Board
Rolands Legzdiņš

CONSOLIDATED AND SEPARATE STATEMENT OF CHANGES IN SHAREHOLDER'S EQUITY

	Note	Share capital	Share premium	Other reser-ves	Reva-luation reserve	Retai-ned ear-nings	Total
Balance at 1 January 2017		**11,664**	**6,360**	**25**	**670**	**42,038**	**57,095**
Total comprehensive income							
Profit for the year		-	-	-	-	(3,429)	(3,429)
Other comprehensive income		-	-	-	(454)	-	(454)
Transactions with shareholders recorded directly in equity							
Dividends paid		-	-	-	-	(20,000)	(20,000)
Balance at 31 December 2017		**11,644**	**6,360**	**25**	**216**	**18,609**	**36,854**
Change in the result of initial application of IFRS 9 (see Note 3 c)		-	-	-	-	(8)	(8)
Balance at 1 January 2018		**11,644**	**6,360**	**25**	**216**	**18,601**	**36,846**
Total comprehensive income							
Profit for the year		-	-	-	-	318	318
Other comprehensive income		-	-	-	(176)	-	(176)
Balance at 31 December 2018		**11,644**	**6,360**	**25**	**40**	**18,919**	**36,988**

The accompanying notes on pages 17 to 73 form an integral part of these financial statements.The financial statements as set out on pages 13 to 73 were approved for issue by the Management Board on 6 March 2019.

Chairman of the
Management Board
Gints Čakāns

Deputy Chairperson of the
Management Board
Evija Sloka

Member of the
Management Board
Rolands Legzdiņš

6 March 2019

NOTES TO THE FINANCIAL STATEMENTS

1 Background

Information on the Bank

AS Expobank (hereinafter the "Bank") was established in the Republic of Latvia on 6 December 1991 as a closed joint stock company. The Bank operates under a credit institution license issued by the Financial and Capital Market Commission of the Republic of Latvia according to which the Bank is allowed to provide all financial services.

In 2018, the Bank continues its operations and development by offering Bank's services to corporate clients and private persons. The services offered by the Bank include current accounts, deposits, lending, local and international money transfers, remote banking, escrow accounts, currency exchange, documentary operations, transactions with securities, brokerage services and payment cards.

The Financial and Capital Market Commission of the Republic of Latvia regulates the Bank's operations.

The Bank's branch in the Republic of Cyprus began its operations in 8 October 2010. In 2018, the Bank made a decision to close the Cyprus branch and as of 18 October 2018, it does not provide financial services to clients. In 2018, the closure processes of the Bank's Luxembourg branch and the Bank's representative office in Hong Kong (China), which were initiated in 2017, were concluded and these foreign units were removed from the relevant public registers.

Information about the Bank:	AS Expobank
Address:	Valdemara street 19, Riga, LV-1010, Latvia
Information about the branch (does not provide financial services as of 18 October 2018):	AS Expobank Cyprus Branch
Address:	Agiou Athanasiou, 46, INTERLINK HERMES PLAZA, 1st floor, Flat/ Office 101B, 4102, Limassol, Cyprus

The Bank has no subsidiaries.

Shareholders

The sole shareholder of the Bank is Igor Kim.

Related party transactions are disclosed in Note 29.

2 Basis of preparation

(1) Statement of compliance

The accompanying financial statements of the Bank have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union ("EU IFRS"), and regulations of the Financial and Capital Market Commission of the Republic of Latvia in force as at the reporting date.

The financial statements were approved for issue by the Management Board on 6 March 2019.

The shareholder has the right to reject these financial statements and request that new financial statements are prepared.

NOTES TO THE FINANCIAL STATEMENTS

2 Basis of preparation, continued

(2) Basis of measurement

The accounting system of the Bank is organised in accordance with the legislation of the Republic of Latvia, including requirements applicable to credit institutions operating in Latvia. The financial year of the Bank coincide with the calendar year.

The financial statements have been prepared on a historical cost basis, except financial assets measured at fair value through other comprehensive income.

(3) Functional and Presentation Currency

The financial statements are presented in thousands of euro (‘000 EUR), unless stated otherwise, being the functional currency of the Bank.

3 Significant accounting policies

The following significant accounting policies have been consistently applied in the preparation of the financial statements, apart from the accounting policy changes resulting from the adoption of IFRS 9 and IFRS 15 effective from 1 January 2018.

(1) Foreign currency

Transactions in foreign currencies are translated into the respective functional currency of the operation at exchange rates published by the European Central Bank at the dates of the transactions. The foreign currency gain or loss on monetary items is the difference between amortized cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortized cost in foreign currency translated at the exchange rate at the end of the period.

Monetary assets and liabilities, including funds under trust management, contingent liabilities and commitments, denominated in foreign currencies at the reporting date are translated into the functional currency at the spot exchange rate at that date. Foreign currency differences arising on translation are recognized in profit and loss, except for differences arising on the translation of financial assets measured at fair value through other comprehensive income.

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 when the fair value was determined.

Exchange rates as of 31 December 2018 and 31 December 2017 were as follows:

	31 December 2018	**31 December 2017**
EUR/USD	0,8734	0,8338
EUR/RUB	0,0125	0,0144
EUR/GBP	1,1179	1,1271

(2) Cash and cash equivalents

Cash and cash equivalents include notes and coins on hand, unrestricted balances held with central banks 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 Bank in the management of their short-term commitments, and deposits and balances due to financial institutions with original maturity less than 3 months (See Note 12).

NOTES TO THE FINANCIAL STATEMENTS

3 Significant accounting policies, continued

(3) Financial assets and financial liabilities

Initial recognition and measurement

Financial assets and financial liabilities are recognised when the entity becomes a party to the contractual provisions of the instrument. Regular way purchases and sales of financial assets are recognised on settlement date, the date on which the asset is delivered to or by the Bank.

At initial recognition, the Bank measures a financial asset or financial liability at its fair value plus or minus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are incremental and directly attributable to the acquisition or issue of the financial asset or financial liability, such as fees and commissions. Transaction costs of financial assets and financial liabilities carried at fair value through profit or loss are expensed in profit or loss. Immediately after initial recognition, an expected credit loss allowance (ECL) is recognised for financial assets measured at amortised cost and investments in debt instruments measured at FVOCI, which results in an accounting loss being recognised in profit or loss when an asset is newly originated.

When the fair value of financial assets and liabilities differs from the transaction price on initial recognition, the entity recognises the difference as follows:

(a) When the fair value is evidenced by a quoted price in an active market for an identical asset or liability (i.e. a Level 1 input) or based on a valuation technique that uses only data from observable markets, the difference is recognised as a gain or loss.

(b) In all other cases, the difference is deferred and the timing of recognition of deferred day one profit or loss is determined individually. It is either amortised over the life of the instrument, deferred until the instrument's fair value can be determined using market observable inputs, or realised through settlement.

Classification

Financial assets at initial recognition are classified in the following measurement categories:

- Financial assets measured at amortised cost (AC);
- Financial assets measured at fair value through d other comprehensive income (FVOCI);
- Financial assets measuredat fair value through profit or loss (FVPL);

Classification of the financial assets is performed based on the following:

- Business model for managing financial assets;
- Characteristics of the contractual cash flows of the financial asset.

The financial assets are measured at amortised cost if the following two conditions are met:

- The financial asset is held within a business model whose objective is to hold financial assets in order to collect ontractual cash flows, and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on principal amount outstanding.

Financial assets are measured at fair value through other comprehensive incomes (i.e., capital reserve), if the following conditions are met:

- The financial asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on principal amount outstanding.

Financial assets are measured at fair value through profit or loss unless it is measured at amortised cost or at fair value through other comprehensive income. The Bank may made an irrevocable election at initial recognition for particular investments in equity instruments that would otherwise be measured at fair value through profit or loss to present subsequent changes in fair value in other comprehensive income.

3 Significant accounting policies, continued

Financial assets measured at fair value through other comprehensive income

Debt instruments

Debt instruments are those instruments that meet the definition of a financial liability from the issuer's perspective, such as loans, government and corporate bonds.

The Bank classifies its debt instruments into the measurement category:

Fair value through other comprehensive income (FVOCI): Financial assets that are held for collection of contractual cash flows and for selling the assets, where the asset's cash flow represents solely payments of principal and interest, and that are not designated at FVPL, are measured at fair value through other comprehensive income (FVOCI). Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses, interest revenue and foreign exchange gains and losses on the instruments amortised cost which are recognised in profit or loss. When the financial asset is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to profit or loss. Interest income from these financial assets is included in "Interest income" using the effective interest method.

Equity instruments

Equity instruments are instruments that meet the definition of equity from the issuer's perspective; that is, instruments that do not contain a contractual obligation to pay and that evidence a residual interest in the issuer's net assets. Examples of equity instruments include basic ordinary shares.
The Bank subsequently measures all equity investments at fair value through profit or loss, except where the Bank's management has elected, at initial recognition, to irrevocably measure an equity investment at fair value through other comprehensive income. The Bank's policy is to designate equity investments at fair value
through other cmpomprehensive income when those investments are held for purposes other than to generate investment returns. When this election is used, fair value gains and losses are recognised in OCI and are not subsequently reclassified to profit or loss, including on disposal. Impairment losses (and reversal of impairment losses) are not reported separately from other changes in fair value. Dividends, when representing a return on such investment and the right to receive payments is established, is recognised in profit or loss.

Financial assets measured at fair value through profit or loss

Derivative financial instruments

Derivative financial instruments include currency swaps and forward contracts.

Derivatives are initially recognized at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. All derivatives are carried as assets when their fair value is positive and as liabilities when their fair value is negative.

Changes in the fair value of derivatives are recognized immediately in the statement of comprehensive income.

Derivatives may be embedded in another contractual arrangement (a "host contract"). An embedded derivative is separated from the host contract and it is accounted for as a derivative if, and only if the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract, a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and the combined instrument is not measured at fair value with changes in fair value recognized in the statement of comprehensive income. Derivatives embedded in financial assets or financial liabilities at fair value through profit or loss are not separated.

Although the Bank trades with derivative instruments for risk hedging purposes, the Bank does not adopt hedge accounting.

NOTES TO THE FINANCIAL STATEMENTS

3 Significant accounting policies, continued

Financial assets and financial liabilities measured at amortized cost

A financial asset or liability is initially measured at its fair value plus, in the case of a financial asset or liability not 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, including derivatives that are assets, are measured at their fair values, without any deduction for transaction costs that may be incurred on sale or other disposal, except for:

- loans and receivables that are measured at amortized cost using the effective interest rate method;
- investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured which are measured at cost.

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 amortized cost. Amortized 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 amortized based on the effective interest rate of the instrument.

Financial assets measured at amortised cost

Demand deposits with central banks, placements with financial institutions and loans and advances due from customers are classified as financial assets measured at amortised cost, provided that the following criteria are met:

- they are held within a business model whose objective is achieved by collecting contractual cash flows ("Held to collect" business model);
- their contractual cash flows represent solely payments of principal and interest on principal amount outstanding
- the Bank does not designate them on initial recognition to fair value through profit or loss measurement option.

Financial assets meeting the aforementioned criteria are measured at amortised cost and are subject to IFRS 9 impairment model.

Financial liabilities measured at amortised cost

All financial liabilities are recognised initially at fair value and, in the case of loans and borrowings, net of directly attributable transaction costs. After the initial recognition, the interest-bearing financial liabilities are recognised at amortised cost using the EIR method. Gains and losses are recognised in profit or loss when the liabilities are derecognised as well as through the EIR method. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. The EIR amortisation is included as net interest income in the statement of profit and loss.

Amortised cost and effective interest rate

The amortised cost is the amount at which the financial asset or financial liability is measured at initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any loss allowance.

NOTES TO THE FINANCIAL STATEMENTS

3 Significant accounting policies, continued

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability to the gross carrying amount of a financial asset (i.e. its amortised cost before any impairment allowance) or to the amortised cost of a financial liability. The calculation does not consider expected credit losses and includes transaction costs, premiums or discounts and fees and points paid or received that are integral to the effective interest rate, such as origination fees.

When the Bank revises the estimates of future cash flows, the carrying amount of the respective financial assets or financial liability is adjusted to reflect the new estimate discounted using the original effective interest rate. Any changes are recognised in profit or loss.

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. The fair value of a liability reflects its non-performance risk.

When available, the Bank measures the fair value of a financial instrument using quoted prices in an active market for that instrument. A market is regarded as 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 Bank establishes fair value using a valuation technique. Valuation techniques include using 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 makes maximum use of market inputs, relies as little as possible on estimates specific to the Bank, incorporates all factors that market participants would consider in setting a price, and is 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 Bank calibrates valuation techniques and tests them for validity using prices from observable current market transactions in the same instrument or based on other available observable market data.

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 in 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 recognized in statement of comprehensive income 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.

Assets and long positions are measured at a bid price; liabilities and short positions are measured at an asking price. Where the Bank has positions with offsetting risks, mid-market prices are used to measure the offsetting risk positions and a bid or asking price adjustment is applied only to the net open position as appropriate. Fair values reflect the credit risk of the instrument and include adjustments to take account of the credit risk of the counterparty where appropriate. Fair value estimates obtained from models are adjusted for any other factors, such as liquidity risk or model uncertainties; to the extent that the the Bank believes a third-party market participant would take them into account in pricing a transaction.

A number of the Bank's accounting policies and disclosures require the determination of fair value of financial assets and liabilities. The methods described below have been used for the determination of fair values. When applicable, further information about the assumptions made in determining fair values is disclosed in the respective notes.

The fair value of shares (S.W.I.F.T) and other non-fixed income securities is determined by reference to their quoted bid price at the reporting date, if available. For a non-material amount of non-listed shares, where disposal opportunities are limited, the assumption has been made that the reliable estimate of fair value is not possible.

The fair value of S.W.I.F.T shares was determined based on the "transfer amount" approved for the respective year by the shareholder's meeting, that represents the price for new share allocation and participants quit price.

NOTES TO THE FINANCIAL STATEMENTS

3 Significant accounting policies, continued

Derecognition of financial assets and liabilities

The Bank derecognises financial assets when (a) the assets are redeemed or the rights to cash flows from the assets otherwise expired or (b the Bank has transferred the rights to the cash flows from the financial assets or entered into a qualifying pass-through arrangement while (i) also transferring substantially all risks and rewards of ownership of the assets or (ii) neither transferring nor retaining substantially all risks and rewards of ownership, but not retaining control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose restrictions on the sale.

The Bank also derecognize certain assets when they write off balances pertaining to the assets deemed to be uncollectible.

A financial asset (or, where applicable a part of a financial asset or a part of a group of similar financial assets) is derecognised when:

- the rights to receive cash flows from the asset have expired; or
- the Bank has transferred the rights to receive cash flows from the asset, or retained the right to receive cash flows from the asset, but have assumed an obligation to pay them in full without material delay to a third party under a ‘pass-through’ arrangement; and
- the Bank either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but have transferred control of the asset.

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

When the contractual cash flows of a financial assets are substantially modified, such a modification is treated as a derecognition of the original assets and the recognition of a new financial asset, and the difference in respective carrying amounts is recognised in the income statement. In the case of financial asset modification, which does not lead to derecognition, the Bank recalculates the gross carrying amount of the financial asset and recognises a modification gain or loss.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or when the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in the income statement.

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 statement of financial position and the counterparty liability included in amounts payable under repo transactions. The difference between the sale and repurchase price represents interest expense and is recognized 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 agreement to resell are sold to third parties, the obligation to return securities is recorded as a trading liability and measured at fair value.

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 recognized amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

NOTES TO THE FINANCIAL STATEMENTS

3 Significant accounting policies, continued

(4) Property and equipment

Items of property and equipment are stated at cost, net of accumulated depreciation and impairment losses, if any.

When an item of property and equipment comprises major components having different useful lives, they are accounted for as separate items of property and equipment.

Depreciation is charged to the income statement on a straight-line basis over the estimated useful lives of the individual assets. Depreciation commences on the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and ready for use. Land is not depreciated.

The estimated useful lives are as follows:

Furniture and equipment	2 to 10 years
Computers and equipment	4 years
Software inseparable from equipment (OEM software)	4 years

Leasehold improvements are capitalised and depreciated over the remaining lease period on a straight-line basis. Leasehold improvements are not depreciated as long as the respective assets are not completed.

An item of property and equipment is derecognized upon disposal or when the asset is no longer in use and no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset calculated as the difference between the net disposal proceeds and the carrying amount of the item upon disposal is included in the statement of comprehensive income.

Depreciation methods, useful lives, and residual values are reviewed annually.

(5) Intangible assets

Intangible assets are identifiable non-monetary assets without physical substance (licences and software that are separately identifiable from electronic devices, etc.) held for rendering of services or other purposes if it is expected that an economic benefit attributable to these assets will flow to the Bank.

Intangible assets are stated at cost less accumulated amortisation and impairment losses and are amortized over the useful life of the asset. The useful life of each class of intangible assets is estimated, considering the

contractual conditions, and/or based on the estimated period over which the asset is expected to generate economic benefits.

The estimated useful lives are as follows:

Software	5 years
Mastercard licence	10 years
Other licences	5 years

Licences acquired by the Bank for a period up to one year are expensed as acquired.

Amortisation methods and useful lives are reviewed annually.

(6) Leased assets and lease payments

Financial lease

Where the Bank is a lessor in a lease which transfers substantially all the risks and rewards incidental to ownership to the lessee, the assets leased out are presented as a finance lease receivable and carried at the present value of the future lease payments. Finance lease receivables are initially recognised at commencement (when the lease term begins) using a discount rate determined at inception (the earlier of the date of the lease agreement and the date of commitment by the parties to the principal provisions of the lease).

The difference between the gross receivable and the present value represents unearned finance income. This income is recognised over the term of the lease using the net investment method (before tax), which reflects a constant periodic rate of return. Incremental costs directly attributable to negotiating and arranging the lease are included in the initial measurement of the finance lease receivable and reduce the amount of income recognised over the lease term. Finance income from leases is recorded within in profit or loss for the year.

NOTES TO THE FINANCIAL STATEMENTS

3 Significant accounting policies, continued

Operating lease

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any financial incentives received from the lessor) are charged to the profit and loss account on a straight-line basis over the period of the lease.

(7) Impairment of financial assets

The following financial instruments are subject to IFRS 9 impairment requirements:

- financial assets measured at amortised cost,
- debt instruments measured at FVOCI,
- contract assets,
- loan commitments and financial guarantee contracts.
-

For financial instruments, which are in scope of impairment model, loss allowances for expected credit losses are calculated in the following way:

- Financial instruments with no significant increase in credit risk since the initial recognition (or financial instruments which are considered to have low credit risk) – loss allowances for expected credit losses are calculated at an amount equal to 12-month expected credit losses,
- Non credit-impaired financial instruments with significant increase in credit risk since the initial recognition -– loss allowances for expected credit losses are calculated at an amount equal to lifetime expected credit losses,
- Credit-impaired financial instruments – loss allowances for expected credit losses are calculated at an amount equal to lifetime expected credit losses,
- Purchased or originated credit-impaired assets (POCI) – loss allowances for expected credit losses are calculated at an amount equal to lifetime expected credit losses regardless of the changes in credit risk during the lifetime of financial assets.

Credit loss is the difference between all contractual cash flows that are due in accordance with the contract and all the cash flows that the Bank expects to receive (i.e. all cash shortfalls), discounted at the original effective interest rate (or credit-adjusted effective interest rate for purchased or originated credit-impaired financial assets). The Bank estimates cash flows by considering all contractual terms of the financial instrument (for example, prepayment, extension, call and similar options) through the expected life of that financial instrument. The cash flows that are considered includes cash flows from the sale of collateral held or other credit enhancements that are integral to the contractual terms.

Expected credit losses are the weighted average of credit losses with the respective risks of a default occurring as the weights. Lifetime expected credit losses are the expected credit losses that result from all possible default events over the expected life of a financial instrument. 12-months expected credit losses are the portion of lifetime expected credit losses that represent the expected credit losses that result from default events on a financial instrument that are possible within the 12 months after the reporting date.

The Bank assesses at each reporting date whether the credit risk on a financial instrument has increased significantly since initial recognition by analysing the change in the risk of a default occurring over the expected life of the financial instrument.

To make that assessment, the Bank compares the risk of a default occurring on the financial instrument as at the reporting date with the risk of a default occurring on the financial instrument as at the date of initial recognition and consider reasonable and supportable information, that is available without undue cost or effort, that is indicative of significant increases in credit risk since initial recognition.

NOTES TO THE FINANCIAL STATEMENTS

3 Significant accounting policies, continued

(7) Impairment of financial assets, continued

For a financial asset that is credit-impaired at the reporting date, but that is not a purchased or originated credit-impaired financial asset, the Bank measures the expected credit losses as the difference between the asset's gross carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. Any adjustment is recognised in profit or loss as an impairment gain or loss.

A financial asset is credit-impaired when one or more events that have a detrimental impact on the estimated future cash flows of that financial asset have occurred. Evidence that a financial asset is credit-impaired include observable data about the following events:

- significant financial difficulty of the issuer or the borrower;
- a breach of contract, such as a default or past due event;
- the lender(s) of the borrower, for economic or contractual reasons relating to the borrower's financial difficulty, having granted to the borrower a concession(s) that the lender(s) would not otherwise consider;
- it is becoming probable that the borrower will enter bankruptcy or other financial reorganisation;
- the disappearance of an active market for that financial asset because of financial difficulties; or
- the purchase or origination of a financial asset at a deep discount that reflects the incurred credit losses.

It may not be possible to identify a single discrete event — instead, the combined effect of several events may have caused financial assets to become credit-impaired.

Financial guarantees and loan commitments are also within the scope of expected credit loss model. For loan commitments, the Bank considers changes in credit risk of the loan to which a loan commitment relates. For financial guarantee contracts, the Bank considers the changes in the risk that the specified debtor will default on the contract.

(8) Taxation

Until 31 December 2016 the Bank recognized and measured the deferred income tax and disclosed information about the deferred income tax in the financial statements in accordance with IAS 12 "Income tax".

On July 28, 2017, a new Corporate Income Tax Law was adopted, which stipulates that from January 1, 2018, the corporate income tax is levied on profit that arose after 2017 if it is distributed or conditionally distributed profit arise. When the law came into force, there were no longer any reason for the existence of a deferred tax asset or liability and in 2017, and the Bank eliminated previously recognized deferred tax liability from the balance sheet, including a reduction in that liability in the profit and loss account for the year 2017.

Legal entities are not required to pay income tax on earned profits starting from 1 January 2018 in accordance with the amendments made to the Corporate Income Tax Law of the Republic of Latvia. Corporate income tax is paid on distributed profits and deemed profit distributions. Starting from 1 January 2018, both distributed profits and deemed profit distributions are subject to the tax rate of 20 per cent of their gross amount, or 20/80 of net expense. Corporate income tax on dividends is recognized in the statement of comprehensive income as expense in the reporting period when respective dividends are declared, whilst for other deemed profit items it is recognized at the time when expense is incurred.

(9) Income and expense recognition

All income and expense categories, including interest income and expense, are recognized on the accrual basis. Income is recognized only to the extent that an inflow of economic benefits to the Bank is possible and such income can be reasonably estimated. Impairment loss is recognized if the receipt of income becomes doubtful.

Interest income and expense are recognized in the income statement using the effective interest rate method. Payments made by the Bank to the deposit guarantee fund are disclosed under other interest expense.

NOTES TO THE FINANCIAL STATEMENTS

3 Significant accounting policies, continued

(9) Income and expense recognition, continued

Loan origination fees and other fees that are considered to be integral to the overall profitability of a loan, together with the related direct costs, are deferred and amortized to interest income over the estimated life of the financial instrument using the effective interest rate method.

Commission and fee income and expense on non-recurring services are recognized on the transaction date on an accrual basis. Commission and fee income and expense on services provided or received in a certain period of time are accrued and charged to the income statement over the period of the services received/rendered.

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

Dividend income is recognized in the statement of comprehensive income on the date that the dividend is declared.

Interest income is calculated by applying the effective interest rate to the gross carrying amount of financial assets.

(10) Employee benefits, continued

Short-term employee benefits, including salaries and social security contributions, bonuses and paid vacation benefits are included in Administrative expenses on an accrual basis.
The Bank pay social security contributions to state pension insurance and to the state funded pension scheme in accordance with Latvian legislation. In accordance with the Rules of the Cabinet of Ministers of Latvia Republic 72% (2017: 72%) of the social security contributions are used to fund the state defined contribution pension system.

State funded pension scheme is a defined contribution plan under which the Bank pay fixed contributions determined by law and will have no legal or constructive obligation to pay further contributions if the state pension insurance system or state funded pension scheme are not able to settle their liabilities to employees. The social security contributions are accrued in the year in which the associated services are rendered by the employees of the Bank.

(11) Use of significant accounting estimates and judgments

The preparation of financial statements in conformity with IFRSs as adopted by the EU requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the 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 judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from those estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized 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:

Impairment of financial assets measured at fair value through other comprehensive income

The determination of impairment indication is based on comparison of the financial instrument’s carrying value and fair value.

For the purposes of impairment loss measurement, the Bank’s management makes estimates of any expected changes in future cash flows from a specific financial instrument based on analysis of financial position of the issuer of the financial instrument.

NOTES TO THE FINANCIAL STATEMENTS

3 Significant accounting policies, continued

(12) Trust operations

The trust operations policy of the Bank set forth the general guidelines on organisation and execution of trust operations, their control and monitoring. The Bank's policy for trust operations is reviewed annually. The

Bank provide trust services only to customers of the Bank.

Trust operations are accounted for separately from the Bank's own operations thus ensuring separate accounting in a separate trust sheet for assets of each customer, by customer and by type of assets under management. The Bank accept no risk for its trust operations; all risk is retained by its customers. The Bank earn fee income for administration of trust operations.

(13) New Standards and Interpretations

(a) Changes in accounting policies

The Bank has 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 Bank did not early adopt any of IFRS 9 in previous periods. As permitted by the transitional provisions of IFRS 9, the Bank elected not to restate comparative figures. Any adjustments to the carrying amounts of financial assets and liabilities at the date of transition were recognised in the opening retained earnings and other reserves 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.

The adoption of IFRS 9 has resulted in changes in our accounting policies for recognition, classification and measurement of financial assets and financial liabilities and impairment of financial assets. IFRS 9 also significantly amends other standards dealing with financial instruments such as IFRS 7 Financial Instruments: Disclosures.

Set out below are disclosures relating to the impact of the adoption of IFRS 9 on the Bank. Further details of the specific IFRS 9 accounting policies applied in the current period (as well as the previous IAS 39 accounting policies applied in the comparative period) are described in more detail below.

(b) Classification and measurement of financial instruments

The measurement category and the carrying amount of financial assets and liabilities in accordance with IAS 39 and IFRS 9 at 1 January 2018 are compared as follows:

Financial assets	Original measurement category under IAS 39	New measurement category under IFRS 9	IAS 39 carrying amount 31 December 2017 EUR'000	New carrying amount under IFRS9 1 January 2018 EUR'000
Cash and demand deposits with the central banks	Loans and receivables	Amortised cost	73,724	73,724
Due from financial institutions	Loans and receivables	Amortised cost	122,620	122,614
Loans and advances due from customers	Loans and receivables	Amortised cost	8	8
Available for sale financial instru-ments	Available for sale	Fair value through other comprehensi-ve income	28,223	28,223
Other assets	Loans and receivables	Amortised cost	1,463	1,461

There were no changes to the classification and measurement of financial liabilities.

The Bank performed a detailed analysis of its business models for managing financial assets and analysis of their cash flow characteristics.

NOTES TO THE FINANCIAL STATEMENTS

3 Significant accounting policies, continued

(c) Reconciliation of statement of financial position balances from IAS 39 to IFRS 9

The following table reconciles the carrying amounts of financial assets, from their previous measurement category in accordance with IAS 39 to their new measurement categories upon transition to IFRS 9 on 1 January 2018:

Financial assets	**IAS 39 carrying amount 31 December 2017**	**Reclassifi-cations**	**Remeasure-ments 31 December 2017**	**IFRS 9 carrying amount 1 January 2018**
Amortised cost				
Cash and demand deposits with the central banks				
Opening balance under IAS 39 and closing balance under IFRS 9	73,724	-	-	73,724
Due from financial institutions				
Opening balance under IAS 39	122,620	-	-	-
Remeasurement (ECL allowances)	-	-	(6)	-
Closing balance under IFRS 9	-	-	-	122,614
Loans and advances due from customers				
Opening balance under IAS 39	8	-	-	-
Remeasurement (ECL allowances)	-	-	-	-
Closing balance under IFRS 9	-	-	-	8
Other assets				
Opening balance under IAS 39	1,463	-	-	-
Remeasurement (ECL allowances)	-	-	(2)	-
Closing balance under IFRS 9		-	-	1,461
Financial assets measured at amortised cost - total	**196,352**	**-**	**(8)**	**196,346**
Fair value through other comprehensive income				
Investments in equity instruments				
Opening balance under IAS 39 and closing balance under IFRS 9	41	-	-	41
Investments in debt instruments				
Opening balance under IAS 39 and closing balance under IFRS 9	28,182	-	-	28,182
Assets at fair value through other comprehensive income - total	**28,223**	**-**	**-**	**28,223**

Financial assets previously classified as available for sale have been reclassified to new category "Financial assets at fair value through other comprehensive income" under IFRS9 as their previous category under IAS39. were "retired", with no changes to their measurement basis.

NOTES TO THE FINANCIAL STATEMENTS

3 Significant accounting policies, continued

(d) Impairment allowance

IFRS 9 fundamentally changed the credit loss recognition methodology. The standard replaced IAS 39's incurred loss approach with a forward-looking expected credit loss (ECL) approach. The Bank is required to recognize an allowance for expected losses for all loans and other debt financial assets not held at FVPL, together with loan commitments and financial guarantee contracts. The allowance is based on the expected credit losses associated with the probability of default in the next twelve months unless there has been a significant increase in credit risk since origination, in which case, the allowance is based on the probability of default over the life of the asset.

(e) Impairment calculation

The Bank performs calculation of ECL (expected credit losses) for the following financial instruments:

- Financial assets measured at amortised cost (AC);
- Financial assets measured at fair value through other comprehensive (FVOCI), except equity securities classified in this category, and
- Off-balance sheet financial liabilities, with inherent credit risk, i.e. financial guarantee contracts and a commitment to issue a loan.

The Bank introduced a three stage model to estimate the expected credit losses.
Stage 1 – financial instruments with no significant increase in credit risk since initial recognition:

- no expected problems with counterparty's obligations in terms of cash flows, as current and future cash flows are sufficient to meet the liabilities;
- financial instruments with low credit risk; the credit risk of a financial instrument is considered low if the financial instrument has low default risk. If a financial instrument has an 'investment grade' (i.e. BBB- and better) external rating, it is considered to have low credit risk.

Stage 2 - financial instruments with a significant increase in credit risk after initial recognition (unless they have low credit risk at the valuation date) but does not have objective evidence of impairment. Regardless of the Bank's assessesment whether the credit risk has increased significantly, if the payments of contractual cash flows are past due more than 30 days, the credit risk of the financial instrument is considered to have increased significantly.

Stage 3 – financial instruments that have objective evidence of impairment at the assessment date, i.e. the financial instrument is in default and/or is assigned a status of a non-performing financial instrument.

Defaults are deemed to have occurred, and the financial instrument is considered as non-performing, if:

- The exposure is past due more than 90 days;
- It is considered that the debtor is unlikely to be able to settle the credit obligations in full without collateral, irrespective of the existence of the overdue amounts and the number of days past due.

Expected credit losses in accordance with IFRS 9

	31.12.2018.		
	Stage 1 EUR'000	**Stage 2 EUR'000**	**Stage 3 EUR'000**
Expected credit loses , total			
Financial assets measured at FVOCI	4	-	-
Loans	-	-	-
Contingent liabilities and commitments	-	-	-
	4	**-**	**-**

The new expected loss approach model had an impact on the Bank's regulatory capital. Upon the decision of the Board of Directors of the Bank, the Bank did not apply transitional arrangements allowed by EU Regulation 2017/2395[1] and recognised the full effect of the implementation of IFRS 9 from 1 January 2018. The capital adequacy ratio is still significantly above the regulatory minimum and in line with the internal Risk Appetite statement.
Adoption of IFRS 9 did not result in breaches of any prudential requirements.

[1] EU Regulation 2017/2395 amends the CRR by introducing Art. 473a on transitional arrangements for mitigating the impact of the introduction of IFRS 9 on own funds

NOTES TO THE FINANCIAL STATEMENTS

3 Significant accounting policies, continued

IFRS 15 "Revenue from Contracts with Customers". The standard is effective for annual periods beginning on or after 1 January 2018. IFRS 15 establishes a five-step model that applies to revenue earned from a contract with a customer (with limited exceptions), regardless of the type of revenue transaction or the industry. The standard's requirements also apply to the recognition and measurement of gains and losses on the sale of some non-financial assets that are not an output of the entity's ordinary activities (e.g., sales of property, plant and equipment or intangibles).

The core principle of IFRS 15 is that revenue must be recognised to reflect the transfer of services to customers at an amount that reflects the consideration that is expected to be received in exchange for such services. This core principle is applied through a five-step model:

1) Identify the contract with the customer,
2) Identify the performance obligation in the contract,
3) Determine the transaction price,
4) Allocate the transaction price to the performance obligation in the contract,
5) Recognise revenue when the performance obligation is satisfied.

For each performance obligation identified the Bank determines at contract inception whether it satisfies the performance obligation over time or at a point in time, whether the consideration is fixed or variable, including whether consideration is constrained due to external factors. Consideration is subsequently allocated to the identified performance obligation.

Management has assessed that the application of the standard did not have effect on the Bank's financial statements.

(f) New standards and interpretations not yet adopted

Amendments to IFRS 2 "Share-based Payment" (effective for annual periods beginning on or after 1 January 2018, not yet endorsed in the EU);

Amendments to IFRS 4 "Insurance Contracts" – Applying IFRS 9 "Financial statements" with IFRS 4 "Insurance contracts" (effective for annual periods beginning on or after 1 January 2018). The amendments address concerns arising from implementing the new financial instruments standard, IFRS 9, before implementing the replacement standard that IASB is developing for IFRS 4. These concerns include temporary volatility in reported results. The amendments introduce two approaches. (1) The amended standard will give all companies that issue insurance contracts the option to recognise in other comprehensive income, rather than profit or loss, the volatility that could arise when IFRS 9 is applied before the new insurance contracts standard is issued ('overlay approach). (2) In addition, the amended standard will give companies whose activities are predominantly connected with insurance an optional temporary exemption from applying IFRS 9 until 2021. The entities that defer the application of IFRS 9 will continue to apply the existing financial instruments standard - IAS 39. The amendments to IFRS 4 supplement existing options in the standard that can already be used to address the temporary volatility

Annual improvements to IFRS's 2016. The amendments include changes that affect 3 standards:

- IFRS 12 "Disclosure of Interests in Other Entities" (effective for annual periods beginning on or after 1 January 2017, not yet endorsed in the EU),
- IFRS 1 "First-time Adoption of International Financial Reporting Standards" (effective for annual periods beginning on or after 1 January 2018, not yet endorsed in the EU), and
- IAS 28 "Investments in Associates and Joint Ventures" (effective for annual periods beginning on or after 1 January 2018, not yet endorsed in the EU).

IFRIC 22 "Foreign Currency Transactions and Advance Consideration" (effective for annual periods beginning on or after 1 January 2018, not yet endorsed in the EU).

Amendments to IFRS 9 "Financial instruments" – Prepayment Features with Negative Compensation (effective for annual periods beginning on or after 1 January 2019, not yet endorsed in the EU).

IFRIC 23 "Uncertainty over Income Tax Treatments" (effective for annual periods beginning on or after 1 January 2019, not yet endorsed in the EU). IAS 12 specifies how to account for current and deferred tax, but not how to reflect the effects of uncertainty. The interpretation clarifies how to apply the recognition and measurement requirements in IAS 12 when there is uncertainty over income tax treatments.

IFRS 16 replaces IAS 17 Leases as of January 1, 2019. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to account for all leases under a single on-balance sheet model similar to the accounting for finance leases under IAS 17. The standard includes two recognition exemptions for lessees – leases of 'low-value' assets (e.g., personal computers) and short-term leases (i.e., leases with a lease term of 12 months or less).

3 Significant accounting policies, continued

At the commencement date of a lease, a lessee will recognise a liability to make lease payments (i.e., the lease liability) and an asset representing the right to use the underlying asset during the lease term (i.e., the right-of-use asset). Lessees will be required to separately recognise the interest expense on the lease liability and the depreciation expense on the right-of-use asset. Lessees will be also required to remeasure the lease liability upon the occurrence of certain events (e.g., a change in the lease term, a change in future lease payments resulting from a change in an index or rate used to determine those payments).

The lessee will generally recognise the amount of the remeasurement of the lease liability as an adjustment to the right-of-use asset.

The main impact the Bank's financial statements will come from the accounting of property leases. Such leasing contract will be accounted for on the balance sheet to a larger extent than today. The right of use assets, presented as "Properties and equipment" on the balance sheet at 1 January 2019, will amount to EUR 882 thousand .

Annual improvements to IFRS's 2017 (effective for annual periods beginning on or after 1 January 2019, not yet endorsed in the EU). The amendments include changes that affect 4 standards:

- IFRS 3 - "Business Combinations", was clarified that an acquirer should remeasure its previously held interest in a joint operation when it obtains control of the business.
- IFRS 11 - "Joint Arrangements", now explicitly explains that the investor should not remeasure its previously held interest when it obtains joint control of a joint operation, similarly to the existing requirements when an associate becomes a joint venture and vice versa.
- IAS 12 - "Income taxes", explains that an entity recognises all income tax consequences of dividends where it has recognised the transactions or events that generated the related distributable profits, eg in profit or loss or in other comprehensive income. It is now clear that this requirement applies in all circumstances as long as payments on financial instruments classified as equity are distributions of profits, and not only in cases when the tax consequences are a result of different tax rates for distributed and undistributed profits.
- IAS 23 - "Borrowing costs", now includes explicit guidance that the borrowings obtained specifically for funding a specified asset are excluded from the pool of general borrowings costs eligible for capitalisation only until the specific asset is substantially complete.

4 Risk and capital management

The Bank's activities results in exposure to a variety of financial and non-financial risks. The Bank's strategic aim is to achieve an appropriate balance between risks assumed by the Bank and returns and minimize the potential adverse effect on the Bank's financial performance and operations.

The risk management system is integrated in the framework of the Bank's internal control based on the effective bank supervision requirements laid down by the Financial and Capital Market Commission and the Basel Committee on Banking Supervision to provide for a risk control function and operational compliance control function independent from business units. Risk measurement, assessment and control functions are separated from the business unit (risk acceptance) functions.

The Bank identifies all inherent significant risks and develop documents and implement appropriate policies for risk management, including measurement, assessment, control, mitigation, and risk reporting and disclosures. Policies are reviewed at least on an annual basis in line with changes in the Bank's operations and external factors impacting the Bank's activities.

In order to identify risks in due time and completely and assess the acceptable levels of risks prior to launching new products and services the Bank assess the potential inherent risks and approves internal normative documents related to risk management that include appropriate procedures, restrictions and limits, and hedging methods. The most important types of risk are credit risk, concentration risk, liquidity risk, interest rate risk, foreign currency and market prices risk, operational risk, money laundering and terrorism financing (further – AML) risk and business model risk (strategic and business risk).

Concentration risk is closely related to different risks of the Bank and assessments are carried out as part of risk management of these risks. The Bank identifies and assesses strategy and business risk, reputational risk and compliance risk. The impact of these risks has been taken into account during strategic planning.

NOTES TO THE FINANCIAL STATEMENTS

4 Risk and capital management, continued

(1) Credit risk

Credit risk represents the Bank's exposure to potential loss in case a borrower (debtor) or a business partner fails or refuses to fulfil its contractual liabilities towards the Bank. The Bank is exposed to credit risk which is a significant inherent risk for the Bank. Therefore, credit risk management is performed with particular care.

Sources of credit risk

The key source for credit risk of the Bank is amounts due from credit institutions, which represent a material asset for the Bank. Credit risk exists also in connection with lending operations, investments in securities, letters of credit and warranties/guarantees.

For the Bank mostly as a payment bank, exposure to credit risk may interfere with liquidity management activities as the Bank should maintain sufficient funds on accounts with several principal correspondents to provide necessary customers' payments in relevant currencies, which sometimes causes also significant concentrations with particular counterparties.

Management and control of credit exposures

The Bank ensures ongoing monitoring of concentrations of credit risk especially to individual counterparties or groups of counterparties, and to industries and countries.

The Bank structures the levels of credit risk they undertake by placing limits on the amount of risk accepted in relation to one counterparty, or a group of counterparties, and to geographical and industry segments, and for a specific type of transaction. Such limits are subject to an annual or more frequent review, taking into account changes in the Bank's operations or external circumstances that can affect the Bank's operations.

The credit risk monitoring system applied by the Bank comprises of regular review of the borrower's/ counterparty's credit standing as well as monitoring of the credit ratings granted by the international credit rating agencies, compliance with the contractual terms and conditions, fulfilment of the obligations, collateral control, as well as ongoing limit control.

Limits on exposures to operations with credit institutions and products are considered by the Assets and Liabilities Management Committee and approved by the Management Board. Limits on exposures to non-banks are considered by the Credit Committee and approved by the Management Board or the Board of Directors depending on the authorisation scope.

The Bank performs regular monitoring of the counterparty credit risk and in case a transaction is to be made with a member of a group of counterparties, the Bank would also assess the overall credit risk exposure of the group.

The Bank ensures regular monitoring of the quality of receivables from counterparties/borrowers and the assessment of credit risk is performed by reference to expected loss and the amount of capital required for addressing credit risk.

Exposures to related groups of counterparties and counterparties related to the Bank is also subject to regulatory requirements.

Credit risk mitigation policies

The Bank employs a range of credit risk mitigation methods.

Credit risk arising from issued warranties/guarantees and credit limits attached to payment cards is primarily covered by a pledge of cash on the accounts opened with the Bank.

The funds derived from the sales of the collateral should generally cover the Bank's expenses incurred in the sale of the collaterals (legal expenses, auctions etc.) and the entire amount of the client's debt towards the Bank, including calculated interest (for the entire period of the loan in the event that the term of the loan is shorter than 12 months or for a period of 12 months in the event that the term of the loan exceeds 12 months). Credit risk arising from loans can be mitigated by mortgage. The Bank's exposures to credit institutions and investment firms are usually unsecured.

NOTES TO THE FINANCIAL STATEMENTS

4 Risk and capital management, continued

Quantitative disclosures

Further quantitative disclosures in respect of credit risk are presented in Note 31.

(2) Foreign exchange risk

Foreign exchange risk represents potential loss from revaluation of items of financial position and contingent liabilities and commitments denominated in foreign currencies due to movements in foreign exchange rates.

Foreign exchange risk management process

The foreign exchange risk management policy determines and regulates the tasks to be performed by the Bank's management and structural units and their responsibilities in managing foreign exchange risk, and foreign exchange risk control regulations and mitigation measures relevant for the Bank's transactions in foreign currencies, as well as measurement, reporting and disclosure procedures.

Limits on the foreign exchange open position in a single currency and the total open position in foreign currencies are set both on open currency positions to be maintained during the business day and open positions at the end of the day which are monitored and controlled.

Quantitative disclosures

Further quantitative disclosures in respect of foreign exchange risk are presented in Note 32.

(3) Position (market price) risk

Position risk is the risk of losses of financial instrument position due to changes in the security's price.

Position risk management process

The Bank by creation of securities portfolios is exposed to securities price fluctuations. Position risk management is addressed in Trading and Investment policies, as well as in the procedures and methodologies that set the limits and limitations. The Bank uses Value at Risk (Value-at-Risk) calculation to estimate maximal loss due to fair value change and assess risks by market stress scenarios. See Note 34.

NOTES TO THE FINANCIAL STATEMENTS

4 Risk and capital management, continued

(4) Liquidity risk

Liquidity risk represents the Bank's exposure to significant loss in the event that Bank does not have a sufficient amount of liquid assets to meet legally substantiated claims or overcome unplanned changes in the Bank's assets and/or market conditions on a timely basis.

Liquidity risk management process

The Bank's liquidity risk management policy sets the key principles and processes of liquidity risk management, tasks of management and structural units and their responsibilities in liquidity management and maintenance, methods and conditions, asset and liability management procedure, measures for preventing and managing liquidity crisis, and reporting and disclosure procedure.

Liquidity risk management is performed by the Bank on the basis of the asset and liability management method ensuring a balanced asset and liability term structure and analysing funding concentration.. The Bank manages liquidity risk as an aggregate of market liquidity risk and financing liquidity risk. Where required, the Bank performs operational liquidity management by attracting funds on the interbank market and by entering into foreign exchange swaps (FX SWAP).

The following techniques are used to manage liquidity:

- Assessment and regular analysis of early warning indicators that help identify adverse trends that may impact the Bank's liquidity;
- Cash flow planning;
- Maintenance of a sufficient amount of liquid assets representing at least level set by regulator (60% of the total amount the Bank's liabilities;
- Monitoring of Liquidity Coverage requirement (LCR) set by European Parliament and Council Regulation (EU) No. 575/2013;
- Liquidity risk limits, restrictions (including finance concentration) and liquidity ratios monitoring;
- The Bank creates a liquidity reserve by maintaining a portfolio of available financial assets - financial assets acquired for the purpose of holding indefinitely and gaining interest income and / or profits from the increase in the price of a financial asset and may be sold for liquidity purposes;
- Balancing asset and liability (including contingent liability) term structure.

Once a year, the Bank submits to the regulator a report on the liquidity adequacy assessment process, which involves identifying, assessing, managing of the liquidity risk and assessing the adequacy of the amount of liquidity needed to ensure the Bank's operations.

The Bank calculates the capital requirement for liquidity risk by assessing possible expenses that may arise if additional financing is required to secure the Bank's liabilities.

Quantitative disclosures

Further quantitative disclosures in respect of liquidity risk are presented in Note 33.

(5) Interest rate risk

Interest rate risk represents the Bank's exposure in the event that changes in interest rates have an adverse impact on the Bank's income and expenses and result in a decrease of the Bank's equity.

Interest rate risk arises from:

- repricing risk;
- yield curve risk;
- basis risk;
- optionality risk - the possibility of incurring losses if a financial instrument directly (options) or indirectly (demand deposits, etc.) provides an option to choose.

When assessing interest rate risk, repricing risk and yield curve risk are assessed together as a single element – the maturity mismatch. The maturity mismatch is used as joint element for assessing repricing risk and yield curve risk as part of interest rate risk.

NOTES TO THE FINANCIAL STATEMENTS

4 Risk and capital management, continued

Interest rate risk management process

The interest rate risk management policy states risk management principles, tasks and responsibilities of the Bank's management and structural units in interest rate risk management, interest rate risk measurement, setting of limits, and control processes, stress testing, as well as reporting and disclosure procedures.

The Bank assesses the impact produced by changes in interest rates on the entire Bank's business, as well as transactions belonging to the Bank's trading and non-trading portfolios, and interest rate risk in each currency for which assets or liabilities exceed 5% of the total balance, and all currencies in total.

Interest rate risk control and mitigation are performed through:

- Interest rate risk limits are determined: net annual interest income, interest rates changing in parallel by 1% (or 100 base points), decrease of economic value assuming that unexpected changes in interest rates represent 200 base points.
- Ensuring the structure of interest rate sensitive assets and liabilities is maintained within levels of interest rate risk that are acceptable to the Bank;
- Control of optionality in clients agreements;
- Constant monitoring of changes in the interest rates on the financial instrument and money markets;
- If necessary an interest rate hedge is applied and interest rate options of the Bank's products are limited.

Quantitative disclosures

Further quantitative disclosures in respect of interest rate risk are presented in Note 34.

(6) Operational risk

Operational risk is the risk that the Bank may suffer loss as a result of noncompliant, unsuccessful or incomplete internal processes or due to staff activities and system operations, or due to external impacts, including risks connected with information technologies and legal risks but excluding reputational risk and strategy and business risk.

In order to identify operational risk events promptly and to take appropriate and timely measures to minimize operational risk the Bank has developed and implemented a statistical data base for registering operational risk events on a regular basis. The Bank has implemented a procedure that all employees regardless of their position immediately make entries of operational risk events in the Event Database upon identifying any circumstances that have caused or may cause losses (irrespective of the type) to the Bank or may inflict damage to the Bank's reputation. If required, all operational risk events entered in the Event Database are checked according to the procedures specified in internal documents, and risk mitigation measures are developed and assigned to improve the internal controls.

Operational risk management process

The Operational Risk Management Policy details the tasks to be performed by the Bank's management and structural units and their responsibilities in the operational risk management, the basic principles of the operational risk management system and operational risk management processes, reporting and disclosures. Besides the above policy, operational risk management connected with the Bank's information systems is regulated by Information System Management Policy and Information System Security Management Policy and internal documents that govern the application thereof.

Operational risk management is performed in the Bank as a complex of systemic measures and it includes:

- identification and assessment of operational risks,
- control of operational risks,
- measures to mitigate operational risks,
- set duties, authorities and responsibilities,
- procedure for reporting and disclosures.

The operational risk management system is integrated in the Bank's internal control system and is aimed at effective management of operational risk. The Bank reviews and improves the operational risk management system on a regular basis to reflect changes in the Bank's operations and external circumstances that impact operations.

NOTES TO THE FINANCIAL STATEMENTS

4 Risk and capital management, continued

The control over operational risks in the Bank is performed using the following control procedures:

- systematic assessment of the operational risk management system, including efficiency assessment;
- compliance reviews against normative documents regulating operational risk management;
- assessment of the results of operational risk assessment and stress testing and, if applicable, implementation of corrective measures in the risk management system;
- consistent control over restrictions and limits imposed by internal documents regulating the respective area;
- regular testing of business continuity plans;
- assessment of changes in the Bank's operations and external environment in order to determine the potential impact on the Bank and its business processes;
- providing the Bank's management with reports of various detail and information on operational risk management and non-compliance with procedures, restrictions and limits and key risk indicators (KRI).
- control over the development of new banking products or services and related internal documents in order to identify operational risks on a timely and complete basis, assess the acceptable level of operational risk and make a decision on risk management. Control over compliance with the Bank's procedures during implementation of new products and services.

(7) AML risk

Money Laundering and Terrorist Financing risk (hereinafter – ML/TF risk) – the potential impact on the Bank and the likelihood that the Bank could be manipulated for the purposes of money laundering, terrorism or proliferation financing.

ML/TF Risk Management

The Bank's priorities concerning ML/TF risk management are to ensure that the Bank's operations are in compliance with the regulatory enactments of the Bank and in accordance with the international standards and best practice including the Finance Latvia Association (formerly – Association of Latvian Commercial Banks) guidelines in the area of Money Laundering and Terrorism Financing prevention, to maintain an effective, independent and complex internal control system, verify its operational integrity and functionality on a regular basis, as well as to raise the qualification and core competencies of the Bank's employees.

The Bank's ML/TF risk management strategy regulates an acceptable ML/TF risk level, defines qualitative and quantitative ML/TF risk exposure indicators and their maximum threshold limits which are based on the capacity to tolerate the permissible ML/TF risk that is in turn pre-determined according to the Bank's business strategy and resources allocated for the ML/TF risk management purposes. The Bank regularly controls the ML/TF risk level, evaluates the effectiveness of ML/TF risk management processes, and, if necessary, promptly implements appropriate risk-mitigating measures.

The ML/TF risk management policy sets forth the tasks and responsibilities for the Bank's management team and its structural units, core internal control system principles regarding ML/TF risk management - its elements and measures, risk identification mechanisms, assessment and control process, risk mitigation activities, employee training guidelines, instructions on submitting reports and documents, employee responsibility in implementing the ML/TF risk management requirements as well as the order in which notifications including anonymous reporting if any irregularities and violations of the ML/TF risk management requirements at the Bank (whistleblowing) are carried out.

The Bank's internal control system pertaining to ML/TF risk management has been established according to the Bank's business model and its operations and considering the inherent client, financial services provided, geographic location, and delivery channels ML/TF risk level and scope, as well as considering the personnel, financial and technological resources involved in the ML/TF risk management, the interaction of the ML/TF risk with other risks inherent to the Bank's daily operations along with additional factors that may significantly impact the overall ML/TF risk level for the Bank.

NOTES TO THE FINANCIAL STATEMENTS

4 Risk and capital management, continued

The Bank has established a specific set of criteria according to which a business relationship with a client would not be initiated (or discontinued) declaring a client to be undesirable to the Bank in terms of “unacceptable risk”. The Bank will not render any banking services to clients whose industry and type of business has been recognized by the Bank as causing excessive risk levels considering the Bank does not possess adequate resources and competencies in order to handle such disproportionate risk levels. The Bank will not provide financial services to any individual or legal entity whose registration (domicile) state has been recognized by the Financial Action Task Force – FATF as high-risk jurisdiction or such which will not cooperate in ML/TF prevention (High-risk and Non-cooperative Jurisdictions).

The Bank refrains from engaging in business transactions and banking services that would pose high ML/TF risk. The only exception for rendering such services would be in situations where the Bank has implemented multiple levels of control in efforts to mitigate the inherent transactional risk. The Bank abstains (or discontinues business activities altogether) with such business or customer segments in which the ML/TF risk has been deemed as “high” unless specific risk mitigation measures have been performed in order to downgrade the residual risk level to “moderate”.

For the purposes of ML/TF risk mitigation the Bank applies various automated control systems for its customers and their transactions including the control of the list of clients and countries that are “undesirable” to the Bank, client cash flow control, as well as automated client ML/TF risk scoring and transaction monitoring systems.

(8) Sanctions Risk

Sanctions risk is the affect or the likelihood that the Bank may be used in efforts to violate or circumvent sanctions.

Sanctions Risk Management

The Bank ensures the implementation of the requirements of national sanctions as well as sanctions imposed by international organizations and applies best practice as it relates to efficient execution of its appropriate control measures in both - when it comes to carrying out transactions on behalf of the Bank and when rendering financial services to its clients while refraining from activities where the goal or resulting consequences were intentional violation of sanctions imposed by the Cabinet of Ministers of the Republic of Latvia, Council of United Nations, European Union, Organization for Security and Cooperation in Europe, United States Department of the Treasury, or the Office of Foreign Assets Control.

The Bank refrains from rendering financial services to clients against whom specific financial sanctions have been imposed upon. In addition, the Bank ensures that those individuals have no access to financial assets and financial instruments and performs the freezing of financial assets and financial instruments belonging to such persons.

Bank does not take part in transactions encompassing civil law transactional dealings of any kind involving economic or financial resources or any other assets thereof which are owned by any given state or any of its associated parties that is under the jurisdiction, governance or holding or over which they have effective controls if civil law restrictions have been introduced by the appropriate national legislation in that state.

In servicing its clients and performing customer transaction monitoring, the Bank implements a complex set of measures in order to insure that the financial services provided by the Bank would not be directly or indirectly used to avoid compliance or the fulfilment of any imposed sanctions. The Bank refrains and promptly ceases to do business with individuals and/or legal entities if there is reasonable doubt or evidence of potential violation of sanctions in their economic activity.

In order to comply with the requirements of sanctions and minimize the risk thereof, the Bank utilizes fully automated IT systems and solutions which assist in determining beneficial owners, representatives, authorized officers and business partners of our clients as well as efficiently ensure screening of payments and an ongoing monitoring of all parties involved.

The Bank’s sanctions compliance policy outlines the key principles of internal control system and sanctions risk assessment at the Bank, defines the tasks and responsibilities of the Bank’s management team and structural units, employee rights, responsibilities and accountability, professional qualification and the “fit and proper” standards according to job responsibilities and authority level of all employees, decision making and reporting processes, employee training, instruction on how corporate reports and information disclosure is to be carried out in compliance with implementation of sanctions including the order which ensures anonymous reporting of any violations involving the fulfilment of sanctions requirements at the Bank (whistleblowing).

NOTES TO THE FINANCIAL STATEMENTS

4 Risk and capital management, continued

(9) Capital management

The strategic objective of the Bank's capital management is to maintain the adequate capital base that would promote attaining the strategic business goals set by the Bank, that is:

- comply with the regulatory requirements;
- be sufficient and optimal to support and further development of the Bank's business in terms of both volume and structure;
- ensure that the Bank's capital, which, based on the internal calculations, is required to cover risks and to establish the capital reserve, both existing and potential, inherent in the current and future business of the Bank, is sufficient to cover significant inherent risks and establish the capital reserve in terms of amount, components and proportion.

The Law on Credit Institutions and the regulations developed by the Financial and Capital Market Commission to apply the provisions of this Law require that the Bank maintain equity that at all times is equal to or exceeds the minimum regulatory capital requirement.

In order to calculate the statutory capital and capital requirement in 2018 and 2017 the Bank applied the rules laid down by REGULATION (EU) No 575/2013 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on prudential requirements for credit institutions and investment firms.

The following table summarises the regulatory capital, capital requirements, and capital adequacy ratios of the Bank as at 31 December 2018 and as at 31 December 2017.

	31.12.2018 EUR'000	**31.12.2017 EUR'000**
Tier 1 capital		
Paid-in share capital	11,644	11,644
Share premium	6,360	6,360
Reserve capital	25	25
Retained earnings	18,601	22,039
Revaluation reserve	40	173
Foreign currency revaluation reserve	-	-
(Loss)/profit for the reporting year	318	(3,429)
Less: investments in non-financial subsidiaries	-	-
Less: value adjustments due to the requirements for prudent valuation	(34)	-
Less: intangible assets	(343)	(456)
Total Tier 1 capital	**36,611**	**36,356**
Subordinated capital (Tier 2)	25	84
Equity used for capital adequacy calculation	**36,636**	**36,440**
Summary of calculations		
Capital requirement for credit risk in the banking book:	(2,420)	(5,435)
Due from central governments and central banks	(386)	-
Due from and contingent liabilities to credit institutions	(394)	(1,730)
Due from and contingent liabilities to companies	(1,582)	(3,567)
Due from and contingent liabilities to retail	-	-
Other items of financial position and contingent liabilities	(58)	(138)
Total capital requirements for market risks, including:	-	-
Capital requirement for currency risk	-	-
Capital requirement traded debt instruments	-	-
Capital requirement for operational risk	(1,598)	(2,178)
Total capital requirement	**(4,018)**	**(7,613)**
Surplus of available equity over capital requirement	**32,619**	**28,827**
Capital adequacy ratio	**72,95%**	**38,29%**

The above is based on internal reports of the Bank, provided to key management of the Bank.

4 Risk and capital management, continued

The Bank's Capital Management Policy lays down the principles of capital management, elements and definition of capital, tasks to be performed by the Bank's management and structural units and their responsibilities, capital management process and its control, reporting and disclosure requirements and actions to be taken by the Bank in emergency situations. The policy requires that the TSCR (the amount of capital needed to cover the risks inherent in the Bank's current and planned operations) ratio always is compliant. The methods used for its assessment of amount of TSCR are more prudent than those used for the calculation of capital as prescribed by law.

Under the current capital requirements provided by the FCMC banks have to maintain a ratio of capital to risk weighted assets ("statutory capital ratio") above the prescribed minimum level. Although the minimum requirement as at 31 December 2018 was 8%, in accordance with a special requirement of the FCMC the Bank had to ensure the capital adequacy above the minimum OCR (the amount of TSCR, the amount of the total recommended capital reserve requirement calculated in Chapter IV of the Credit Institutions Law and the total amount of the recommended recommended capital buffer) ratio level, starting from 1 December 2017– 14.1%. The Bank manages capital by setting the target range for the capital adequacy and OCR ratios, which is treated as a measure of whether the strategic objectives set in capital management have been attained.

The goal of capital management control is to maintain the adequate capital to cover significant risks and keep the reserve on an ongoing basis as well as to comply with the capital adequacy targets set by the Bank. The Bank performs control of the capital management process as a set of systematic measures, defining the relevant control procedures.

5 Net interest income

	2018 EUR'000	2017 EUR'000
Interest income		
Due from financial institutions	414	1,575
Loans and advances due from customers	3	463
Financial assets at fair value through other comprehensive income	685	1,253
	1,102	**3,291**
Interest expense		
Current accounts and deposits due to customers	99	398
Deposits due to financial institutions	146	315
Other interest expense	155	144
	400	**857**

6 Fee and commission income

	2018 EUR'000	2017 EUR'000
Money transfers	1,054	2,364
Trust account servicing	1,183	1,193
Current account servicing	1,456	1,330
Payment cards	106	391
Brokerage fees	357	437
Other	5	25
	4,161	**5,740**

NOTES TO THE FINANCIAL STATEMENTS

7 Fee and commission expense

	2018 EUR'000	2017 EUR'000
Money transfers	51	197
Payment cards	56	113
Brokerage	45	39
Other	12	10
	164	**359**

8 Net income from transactions with financial instruments

	2018 EUR'000	2017 EUR'000
Gain on currency exchange transactions	882	2,683
(Loss)/gain on translation of balances denominated in foreign currencies	(11)	2
Unrealized gain/ (loss) on currency exchange transactions	16	(109)
Gain on financial instruments trading	43	258
Gain on held for trading securities trading	-	2
	930	**2,836**

9 Other expenses

	2018 EUR'000	2017 EUR'000
Association membership fees	146	255
Information services fees	513	674
Professional services	145	425
Other expense	330	21
	1,134	**1,375**

10 General administrative expenses

	2018 EUR'000	2017 EUR'000
Remuneration to staff	1,730	2,502
Remuneration to the Management Board and Board of Directors members	612	844
Statutory social insurance contributions	517	718
Taxes	2	41
Professional services	255	359
Depreciation and amortisation	332	596
Rent expenses	282	283
Security	51	51
Telecommunications	71	80
Transport	1	11
Repairs and maintenance of premises	82	76
Business trips	132	120
Representations	1	2
Sponsorship	-	30
Other expense	434	380
	4,502	**6,093**

NOTES TO THE FINANCIAL STATEMENTS

11 General administrative expenses

The average number of the Bank's employees in 2018 was 65 (2017 - 85). Fee to sworn auditor EUR 41 thousand (2017: 36 thousand).

During the reporting year the sworn auditor's company provided the following non-audit services to the Bank: limited assurance engagements on compliance with the requirements of the Financial Instruments Market Law on the separate maintenance of financial instruments and monetary resources of the Bank and its clients and the requirements of the Deposit Guarantee Law on preparation of the report on guaranteed deposits and payments into deposit guarantee fund.

Income tax expense

(a) Income tax charge

The components of income tax expense for the years ended 31 December 2018 and 2017 were as follows:

	2018 EUR'000	**2017 EUR'000**
Current income tax expense	28	357
Deferred tax expense (see Note 3 (8))	-	(12)
Total	**28**	**345**

12 Cash and deposits with the central banks

	31.12.2018 EUR'000	**31.12.2017 EUR'000**
Cash	57	134
Demand deposits with the Central Banks	13,509	73,590
Total cash and deposits with the Central banks	**13,566**	**73,724**

Since the beginning of 2014 Latvia is a member of European Monetary Union (EMU) and Latvian commercial banks should fulfil all requirements set by the European Central Bank (ECB). In particular ECB set reserve requirement ratio meaning that financial institutions should maintain certain amount of cash with its local Central Bank - in case of AS Expobank with the Bank of Latvia. The Bank's average correspondent account balance should exceed the minimum reserve requirement. The Bank was in compliance with reserve requirement ratio during the reporting year.

13 Cash and cash equivalents

	31.12.2018 EUR'000	**31.12.2017 EUR'000**
Cash and demand deposits with the Central banks	13,566	73,724
Due from financial institutions with original maturity less than 3 months	33,198	122,582
Deposits and balances due to financial institutions with original maturity less than 3 months	(1)	(3,188)
	46,763	**193,118**

NOTES TO THE FINANCIAL STATEMENTS

14 Due from financial institutions

	31.12.2018 EUR'000	31.12.2017 EUR'000
Nostro accounts		
Latvian commercial banks	35	5,285
OECD banks	5,935	12,463
Non-OECD banks	1,339	51,262
Total nostro accounts	**7,309**	**69,010**
Deposits		
OECD banks	16,599	50,274
Non-OECD banks	9,290	3,336
Total deposits	25,889	53,610
Total due from financial institutions	**33,198**	**122,620**

15 Loans and advances due from customers

The breakdown of loans due from customers is as follows:

a) by borrower

	31.12.2018 EUR'000	31.12.2017 EUR'000
Commercial loans		
Credit cards	-	1
Total commercial loans	**-**	**1**
Credit cards	4	7
Total loans to individuals	**4**	**7**
Gross loans and advances due from customers	**4**	**8**
Net loans and advances due from customers	**4**	**8**

(b) by the term of agreement

	31.12.2018 EUR'000	31.12.2017 EUR'000
Up to one year	4	8
Gross loans and advances due from customers	**4**	**8**
Net loans and advances due from customers	**4**	**8**

(c) by industry

	31.12.2018 EUR'000	31.12.2017 EUR'000
Loans to small and medium entities	-	1
Loans to individuals	4	7
Gross loans and advances due from customers	**4**	**8**
Net loans and advances due from customers	**4**	**8**

NOTES TO THE FINANCIAL STATEMENTS

15 Loans and advances due from customers, continued

(d) by geographical region

	31.12.2018 EUR'000	31.12.2017 EUR'000
Latvia	4	7
Non-OECD	-	1
Gross loans and advances due from customers	**4**	**8**
Net loans and advances due from customers	**4**	**8**

Credit quality of commercial loan portfolio and loans to individuals

In the Bank's financial statements no impairment loss has been recognized for commercial loans and loans to individuals as at 31 December 2018 and 31 December 2017. None of the loans were overdue as at 31 December 2018 and 31 December 2017 and all are classified in Stage 1.

(e) by type of collateral

	31.12.2018 EUR'000	31.12.2017 EUR'000
Deposit	-	1
Without collateral	4	7
Gross loans and advances due from customers	**4**	**8**
Net loans and advances due from customers	**4**	**8**

The amounts shown in the table above represent the carrying value of the loans, and do not necessarily represent the fair value of the collateral.

16 Financial instruments

	31.12.2018 EUR'000	31.12.2017 EUR'000
Corporate bonds	33,605	28,182
Private corporations shares	62	41
Total available-for-sale financial assets	**33,667**	**28,223**

NOTES TO THE FINANCIAL STATEMENTS

17 Property and equipment

EUR'000	Leasehold improvements	Other assets	Total
Historical cost			
As at 1 January 2018	153	1,202	1,355
Additions	-	143	143
Disposals	(16)	(158)	(174)
As at 31 December 2018	**137**	**1,187**	**1,324**
Accumulated depreciation			
As at 1 January 2018	131	722	853
Depreciation charge	22	177	199
Disposals	(16)	(93)	(109)
As at 31 December 2018	**137**	**806**	**943**
Net carrying amount			
As at 1 January 2018	**22**	**480**	**502**
As at 31 December 2018	**-**	**381**	**381**
Historical cost			
As at 1 January 2017	194	1,253	1,447
Additions	27	12	39
Disposals	(68)	(63)	(131)
As at 31 December 2017	**153**	**1,202**	**1,355**
Accumulated depreciation			
As at 1 January 2017	102	590	692
Depreciation charge	54	185	239
Disposals	(25)	(53)	(78)
As at 31 December 2017	**131**	**722**	**853**
Net carrying amount			
As at 1 January 2017	**92**	**663**	**755**
As at 31 December 2017	**22**	**480**	**502**

NOTES TO THE FINANCIAL STATEMENTS

18 Intangible assets

EUR'000	Software and licences	
	2018	**2017**
Historical cost		
As at 1 January	1,672	1,558
Additions	29	271
Disposals	(5)	(147)
As at 31 December	**1,696**	**1,682**
Accumulated amortisation		
As at 1 January	1,226	1,066
Amortisation charge	133	176
Disposals	(6)	(16)
As at 31 December	**1,353**	**1,226**
Net carrying amount		
As at 1 January	**446**	**492**
As at 31 December	**343**	**456**

All intangible assets including software are used in the operating activities of the Bank.

19 Other assets

	31.12.2018 EUR'000	31.12.2017 EUR'000
Other financial assets		
Currency exchange transactions in progress	-	1
Credit cards guarantee deposit	176	168
Due from broker accounts	56	878
Other financial assets	-	73
	232	**1,120**
Other non-financial assets		
Prepaid expense	138	181
Accrued income	195	117
Other non-financial assets	74	42
	407	**338**
	639	**1,461**

20 Deposits and balances due to financial institutions

	31.12.2018 EUR'000	31.12.2017 EUR'000
Vostro accounts	1	3,182
Broker accounts	-	9
	1	**3,191**

Concentration of deposits and balances from banks and other financial institutions

As at 31 December 2017, the largest amounts due on demand to Expobank LLC (Russia) and Expobank CZ a.s. amounted to EUR 418 thousand and EUR 2,741 thousand respectively. In 2018, the Bank closed Expobank LLC (Russia) and Expobank CZ a.s. Vostro Accounts.

NOTES TO THE FINANCIAL STATEMENTS

21 Investments in subsidiaries

On 10 August 2017 the Bank sold all shares (100 %) of the subsidiary company Walbrook Capital Markets Limited (reg. No. 2926252, United Kingdom) which is an investment broker company owned by the Bank, including its subsidiary company's Walbrook Capital Markets Nominees Limited (reg. No. 4027520, United Kingdom).

On 29 September 2017, the Bank sold all shares (100 %) of the subsidiary company SIA "Axi Invest" (reģ. Nr. 40103360551, Latvia) owned by the Bank.

On 5 October 2017, the Bank sold all shares (100 %) of the subsidiary company SIA "SIA "Kappa Capital" (reģ. Nr. 40103360547, Latvia) owned by the Bank.

Due to sale of its subsidiaries the Bank has recognised a one-off loss of EUR 6,903 thousand.

22 Current accounts and deposits due to customers

As at 31 December 2018, the largest deposit from one customer with the Bank amounted to EUR 15,928 thousand or 36% of the total deposits respectively (2017: EUR 23,348 thousand or 13%), while the deposit from one group of related customers with the Bank amounted to EUR 16,129 thousand or 36% respectively of the total deposits (2017: EUR 24,447 thousand or 13%).

The breakdown of current accounts and deposits due to customers is as follows:

(a) by the term of the agreement

	31.12.2018 EUR'000	31.12.2017 EUR'000
Current accounts, including accrued interest	26,766	185,712
Deposits:		
up to six months	17,419	-
from six months to one year	100	-
more than one year	346	607
Accrued interest	11	2
Total current accounts and deposits due to customers	**44,642**	**186,321**

(b) by geographical region

	31.12.2018 EUR'000	31.12.2017 EUR'000
Residents of Latvia	1,309	1,825
Non-residents:		
Residents of OECD countries	18,753	23,742
Residents of other countries	24,569	160,754
Total current accounts and deposits due to customers	**44,631**	**186,321**

NOTES TO THE FINANCIAL STATEMENTS

22 Current accounts and deposits due to customers, continued

(c) by depositor

	31.12.2018 EUR'000	31.12.2017 EUR'000
Current accounts		
Residents:		
Private enterprises	794	1,263
Private individuals	512	525
Bank employees	1	37
	1,307	**1,825**
Non-residents:		
Financial institutions	885	22,180
Private enterprises	10,904	155,357
Private individuals	13,634	6,314
Bank employees	36	36
	25,459	**183,887**
Total current accounts	**26,766**	**185,712**
Deposits		
Residents:		
Private enterprises	2	1
	2	**1**
Non-residents:		
Private enterprises	17,439	157
Private individuals	421	430
Financial institutions	3	21
	17,863	**608**
Total deposits	**17,863**	**609**
Total current accounts and deposits due to customers	**44,631**	**186,321**

Interest rates applied to deposits of the Bank's employees do not differ from interest rates on deposits from other customers.

Subordinated liabilities

As at 31 December 2018 the Bank's subordinated liabilities of 302 thousand EUR (2017: 302 thousand EUR) comprised subordinated loan amounting to 300 thousand EUR concluded on 30 May 2014 with interest rate 1% per annum maturing on 29 May 2019. Subordinated loan is included in the second tier of equity calculation and stated at amortised cost. According to the provisions of the subordinated loan agreement, the lender have no right to demand anticipatory repayment of the loans and capitalise the subordinated loans into the Bank's share capital.

NOTES TO THE FINANCIAL STATEMENTS

23 Accrued liabilities

EUR'000	Employee unused holiday pay
As at 31 December 2017	**97**
Increase in provisions	-
As at 31 December 2017	**97**
Increase in provisions	13
As at 31 December 2018	**110**

Management is unaware of any significant actual, pending or threatened claims against the Bank.

24 Other liabilities

	31.12.2018 EUR'000	31.12.2017 EUR'000
Financial liabilities		
Cash in transit	7	222
Currency exchange transactions in progress	-	16
Creditors	5	-
	12	**238**
Non-financial liabilities		
Accrued expense	504	396
	504	**396**
Total other liabilities	**516**	**634**

25 Shareholder's equity

Share capital

As at 31 December 2015, the fully paid-in share capital of the Bank was LVL 8,200 thousand and consisted of 820,000 voting ordinary registered shares with the nominal value of LVL 10 each.

Denominations of paid-in share capital and nominal value of shares from LVL to EUR took place in 2016. As a result paid-in share capital of the Bank is EUR 11 644 thousand, consisted of 820,000 voting ordinary registered shares with nominal value of EUR 14,20 each. The residual value from denomination was reclassified to reserves.

All shares rank equally with regard to the Bank's residual assets, to the right to dividends and to vote at meetings of the Bank. The sole shareholder owning 100% of paid-in share capital is Mr Igor Kim.

Share premium

In 2004, the Bank executed a share capital increase of EUR 4,240 thousand with a share premium of EUR 6,360 thousand.

Revaluation reserve

The revaluation reserve includes the revaluation result of financial assets measured at fair value through other comprehensive income. (2017: available for sale financial assets)

Other reserves

Other reserves comprise the remaining portion of the statutory reserves made from the previous years' profits and residual value from paid-in share capital denomination in 2018. As at 31 December 2018 and 2017 there was no legislative requirement for creation of such reserve.

NOTES TO THE FINANCIAL STATEMENTS

26 Contingent liabilities and commitments

	31.12.2018 EUR'000	31.12.2017 EUR'000
Contingent liabilities		
Guarantees	-	15
	-	**15**
Commitments		
Credit cards commitments	49	192
	49	**192**
Total contingent liabilities and commitments	**49**	**207**

To meet the financial needs of customers, the Bank enters into various transactions resulting in contingent liabilities and commitments. Even though these financial liabilities are not recognized in the statement of financial position, they do contain credit risk and are therefore part of the overall risk assessment of the Bank.

Nevertheless, the potential credit loss is less than the total unused part of the liability since these are contingent upon customers maintaining specific standards. The Bank employs collateral mainly in the form of term deposits for mitigation of related credit risk.

Issued guarantees commit the Bank to make payments on behalf of the customers in the event of a specific act. Other commitments represent contractual obligations on payment cards' overdraft facilities. Since contingent liabilities and commitments may expire without being drawn on, the total contract amount do not necessarily represents future cash requirements.

27 Operating leases

The Bank is a lessee

Where the Bank is a lessee, the breakdown of the future minimum lease payments by periods until the maturity of operating leases effective as at 31 December 2018 are as follows:

EUR'000	Less than one year	Between one and five years	Total
Rent of premises	209	713	922

Where the Bank is a lessee, the breakdown of the future minimum lease payments by periods until the maturity of operating leases effective as at 31 December 2017 are as follows:

EUR'000	Less than one year	Between one and five years	Total
Rent of premises	195	349	544

The leases typically run for an initial period of three to five years, with an option to renew the lease after that date. Lease payments are fixed for the whole lease period. None of the leases includes contingent rentals.

During the current year EUR 202 thousand was recognized as an expense in the income statement in respect of operating leases (2017: EUR 283 thousand).

28 Funds under trust management

The Bank provide Assets under management services to individuals and institutions, where by it holds and manages assets or invests funds received in various financial instruments at the direction of the customer. The Bank receive fee income for providing these services. Assets under management are neither assets of the Bank and are not recognised in the consolidated and separate statement of financial position. The Bank are not exposed to any credit risk relating to such placements, as it does not guarantee these investments.

	31.12.2018 EUR'000	31.12.2017 EUR'000
Assets under management		
Non-residents:		
Loans	74,149	120,913
Placement of resources in financial institutions	-	-
	74,149	**120,913**
Liabilities under management		
Residents:		
Private individuals	-	684
Non-residents:		
Private enterprises	73,129	120,229
Private individuals	1,020	-
	74,149	**120,913**

29 Related party transactions

Related parties are defined as shareholders who have significant influence over the Bank, companies in which such shareholders have controlling interest, members of the Board of Directors and the Management Board, other key management personnel, their close relatives and companies in which they have a controlling interest, as well as associated companies.

The Law on Credit Institutions defines significant investment as a shareholding of 10 or more per cent of the company's capital or voting shares, obtained directly or indirectly, or providing an opportunity to exercise significant influence over the company's activities.

The definition of related parties of the Law on Credit Institutions generally complies with the requirements of IAS 24 as applicable to the Bank which also specifies the requirements for disclosure of related party transactions in the financial statements.

The Bank enters into transactions with related parties in the ordinary course of business. All the loans, advances and financing activities arranged with related parties are at market rates. For the year ended 31 December 2018, all assets are performing and free of any impairment for credit losses (2017: nil).

The Bank's financial statements comprise the following outstanding balances, contingent liabilities and commitments, and statement of comprehensive income items as a result of transactions with related parties:

NOTES TO THE FINANCIAL STATEMENTS

29 Related party transactions, continued

The Bank's statement of financial position

	Key management personnel		Other related parties	
	31.12.2018 EUR'000	**31.12.2017 EUR'000**	**31.12.2018 EUR'000**	**31.12.2017 EUR'000**
Assets				
Due from financial institutions	-	-	-	3,535
Loans and advances due from customers	1	-	-	-
	1	**-**	**-**	**3,535**
Liabilities				
Deposits and balances due to financial institutions	-	-	-	2,738
Current accounts and deposits due to customers	1	39	609	844
	1	**39**	**609**	**3,582**

The Bank's contingent liabilities and commitments

	Key management personnel		Other related parties	
	31.12.2018 EUR'000	**31.12.2017 EUR'000**	**31.12.2018 EUR'000**	**31.12.2017 EUR'000**
Assets under management	-	-	-	684
Liabilities under management	-	684	-	-
Other commitments	20	22	-	-

The Bank's statement of comprehensive income

	Key management personnel		Other related parties	
	2018 EUR'000	**2017 EUR'000**	**2018 EUR'000**	**2017 EUR'000**
Interest income	-	-	2	265
Fee and commission income	1	1	24	109
	1	**1**	**26**	**374**

Detailed information about remuneration to the Management Board and Board of Directors members is disclosed in Note 10.

NOTES TO THE FINANCIAL STATEMENTS

30 Fair value of financial assets and financial liabilities

Set out below is the comparison of the carrying amounts and fair values of the Bank's financial instruments that are recognized in the financial statements.

(a) Financial instruments measured at fair value

The table below analyses financial instruments of 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.

2018	**Level 1 EUR'000**	**Level 2 EUR'000**	**Level 3 EUR'000**	**Total EUR'000**
Financial assets				
Financial assets at fair value through other comprehensive income	33,605	-	62	33,667
	33,605	**-**	**62**	**33,667**
2017				
Financial assets				
Available for sale instruments	28,182	-	41	28,223
	28,128	**-**	**41**	**28,223**

During 2018 there were no reclassification between fair value hierarchy levels.

(b) Financial instruments not measured at fair value

The table below analyses the fair values of the Bank's financial instruments not measured at fair value, by the level in the fair value hierarchy into which each fair value measurement is categorised:

31 December 2018	**Level 1 EUR'000**	**Level 2 EUR'000**	**Level 3 EUR'000**	**Total fair values EUR'000**	**Total carrying amount EUR'000**
Financial assets					
Cash and demand deposits with the central banks	-	-	13,566	13,566	13,566
Due from financial institutions	-	-	33,171	33,171	33,171
Loans and advances due from customers	-	-	4	4	4
Other financial assets	-	-	232	232	232
Financial liabilities					
Deposits and balances due to financial institutions	-	-	44,275	44,275	44,275
Current accounts and deposits due to customers	-	-	364	364	364
Other financial liabilities	-	-	12	12	12

Cash and demand deposits with the Central banks are various currency cash and deposits with the Bank of Latvia and Central Bank of Cyprus whose carrying amount represents the fair value.

Other financial assets consist of cash on broker and escrow accounts, credit card guarantee deposits and currency exchange transactions in progress; thus the carrying amount is equal to their fair value.

Other financial liabilities consist of cash on suspense account and currency exchange transactions in progress; thus the carrying amount is equal to their fair value.

NOTES TO THE FINANCIAL STATEMENTS

30 Fair value of financial assets and financial liabilities, continued

The table below analyses the fair values of the Bank's of financial instruments not measured at fair value, by the level in the fair value hierarchy into which each fair value measurement is categorised:

31 December 2017	Level 1 EUR'000	Level 2 EUR'000	Level 3 EUR'000	Total fair values EUR'000	Total carrying amount EUR'000
Financial assets					
Cash and demand deposits with the Central banks	-	-	73,724	73,724	73,724
Due from financial institutions	-	-	122,600	122,600	122,620
Loans and advances due from customers	-	-	8	8	8
Other financial assets	-	-	1,120	1,120	1,120
Financial liabilities					
Deposits and balances due to financial institutions	-	-	3,191	3,191	3,191
Current accounts and deposits due to customers	-	-	186,320	186,320	186,321
Other financial liabilities	-	-	238	238	238

The methodology for determining the fair value is disclosed in Note 3.

The following table presents interest rates used to discount estimated cash flows, where applicable, by the classes of financial assets and financial liabilities.

	31.12.2018	31.12.2017
Due from and due to financial institutions	-0.117-3.005%	-0.186-2.106%
Loans and advances due from customers	0.00%-3.565%	3.41%-4.10%
Current accounts and deposits due to customers	0.03%-0.45%	0.15%-3.33%

For financial instruments whose fair value is estimated using valuation techniques with non-market observable inputs, net unrealized amount due to changes in the inputs was zero during the year 2018 (2017: nil).

NOTES TO THE FINANCIAL STATEMENTS

31 Credit risk

Maximum credit risk exposure

The table below shows the Bank's maximum exposure to credit risk for the components of the statement of financial position.

The maximum credit exposures are shown both gross, i.e. without taking into account any collateral, provisions and other credit enhancements, and net, i.e. after taking into account any collateral and other credit enhancements.

	Note	Gross maximum credit exposure		Net maximum credit exposure	
		31.12.2018 EUR'000	31.12.2017 EUR'000	31.12.2018 EUR'000	31.12.2017 EUR'000
Cash and demand deposits with the Central banks	12	13,566	73,724	13,566	73,724
Due from financial institutions	14	33,199	122,620	33,198	122,620
Loans and advances due from customers	15	4	8	4	8
Financial assets at fair value through other comprehensive income	16	33,667	28,223	33,667	28,223
Other financial assets	19	232	1,120	232	1,120
Total financial assets		**80,671**	**225,695**	**80,667**	**225,695**
Guarantees	25	-	15	-	15
Credit cards commitments	25	49	192	49	192
Total contingent liabilities and commitments		**49**	**207**	**49**	**207**
Total maximum credit risk exposure		**80,720**	**225,902**	**80,716**	**225,902**

As it is shown above, 41% of the total gross maximum credit exposure is derived from balances due from credit institutions (2017: 54%).

NOTES TO THE FINANCIAL STATEMENTS

31 Credit risk, continued

Concentrations of the maximum credit risk exposure

The following table breaks down the gross exposure related to the Bank’s balances due from credit institutions by geographical regions and major counterparties or groups of related counterparties.

Latvia		31.12.2018 EUR’000	31.12.2017 EUR’000
AS „Swedbank”		35	49
AS „SEB banka”		-	475
Rietumu Bank		-	4,760
Total Latvia		**35**	**5,284**
OECD countries			
Banque et Caisse Depargne	Luxembourg	-	47
Sumitomo Mitsui Banking Corporation	UK, USA, Canada	-	25,018
Raiffeisen Zentralbank International AG	Austria	5,442	11,183
Norddeutsche Landesbank Luxembourg SA	Luxembourg	16,599	25,018
Sumitomo Mitsui Banking Corporation	Japan	-	243
UBI Banka (Unione Di Banche Italiane) S.C.P.A	Italy	447	447
BANK OF CYPRUS	Cyprus	-	1
Euroclear Bank S.A.	Belgium	45	515
Westpac Banking Corporation	USA, UK	-	36
Expobank CZ a.s.	Czech Republic	-	229
Total OECD countries		**22,533**	**62,737**
Other countries			
OAO „Alfa-Bank”	Russia	6,903	4,618
Expobank LLC	Russia	-	3,361
OAO „Sberbank of Russia”	Russia	3,429	6,930
AO “Gazprombank”	Russia	-	3,346
OAO Raiffeisenbank	Russia	280	290
Industrial and Commercial Bank of China (ASIA)	Hong Kong	3	35,921
Industrial and Commercial Bank of China	China	14	43
Bank of China (Russia)	China	1	90
Total other countries		**10,630**	**54,599**
Total balances due from credit institutions		**33,198**	**122,620**

For the Bank the gross maximum credit risk exposure to a single counterparty or a group of related counterparties as at 31 December 2018 comprised 50% and 21% of the total gross credit exposure attributable to balances due from credit institutions (2017: 20% and 29%).

NOTES TO THE FINANCIAL STATEMENTS

31 Credit risk, continued

Credit quality per class of financial assets

Credit quality of financial assets is managed by the Bank by employing debtors' (borrowers') financial analysis techniques, analysis of the counterparty's reputation and historical cooperation with the counterparty, as well as using credit ratings granted by international rating agencies.

The transactions subject to credit risk are divided into four credit quality groups depending on the credit ratings published by international rating agencies. There are the following credit quality groups:

Group 1: AAA, AA (Standard& Poor's, Fitch) / Aaa, Aa (Moody's)

This group includes first class transaction partners who are considered to be low-risk investments. The largest exposure included in this group relates to receivables from Euroclear Bank S.A. (2017: Banque et Caisse d Epargne, Westpac BankingCorporation, Euroclear Bank S.A).

Group 2: A, BBB (Standard& Poor's, Fitch) / A, Baa (Moody's)

This group includes transaction partners with a market position ranging from medium to good. The largest exposure included in this group relates to receivables from Swedbank AS, Industrial and Commercial Bank of China LIMITED, Sumitomo Mitsui Banking Corporation, Industrial and Commercial Bank of China (Asia) (2017: UBI BANCA (UNIONE DI BANCHE ITALIANE) S.C.P.A., Industrial and Commercial Bank of China LIMITED, Sumitomo Mitsui Banking Corporation, Industrial and Commercial Bank of China (Asia), Bank of CHINA (RUSSIA) and NORD / LB Luxembourg Covered Bond Bank).

Group 3: BB, B, CCC, CC, (Standard& Poor's, Fitch) / Ba, B, C (Moody's)

The largest credit risk exposure in this group relates to receivables from transaction partners below medium rating BB (Standard& Poor's, Fitch) / Ba (Moody's). Out of the above group, the most significant receivables are from Raiffeisen Bank International AG, OAO Raiffeisenbank, Norddeutsche Landesbank Luxembourg SA (2017: Sberbank of Russia , Gazprombank, Bank of Cyprus, OAO Raiffeisenbank).

No rating

Transaction partners who have not been assigned an international credit rating are primarily daughter banks of credit institutions operating in the Republic of Latvia. In this group, the largest receivables are from Expobank Cz and Gazprombank.

The table below shows the credit quality by class of financial assets for the Bank as at 31 December 2018 based on international ratings.

EUR'000	Neither past due nor impaired				Total
	Group 1	Group 2	Group 3	No rating	
Cash and demand deposits with the Central banks	-	13,480	29	57	13,566
Due from financial institutions	45	51	33,102	-	33,198
Loans and advances due from customers	-	-	-	4	4
Financial assets at fair value through other comprehensive income	9,323	13,326	10,955	63	33,667
Other financial assets	-	-	-	235	235
Total financial assets, gross	**9,368**	**26,857**	**44,086**	**359**	**80,670**
Less: impairment allowance	-	-	1	3	4
Total financial assets, net	**9,368**	**26,857**	**44,085**	**356**	**80,666**

NOTES TO THE FINANCIAL STATEMENTS

31 Credit risk, continued

The table below shows the credit quality by class of financial assets for the Bank as at 31 December 2017 based on international ratings.

EUR'000	Neither past due nor impaired				Impaired	Total
	Group 1	Group 2	Group 3	No rating		
Demand deposits with the Central banks	30,013	43,549	29	133	-	73,724
Due from financial institutions	599	97,962	18,546	5,213	-	122,620
Loans and advances due from customers	-	-	-	8	-	8
Available-for-sale assets	4,159	10,194	20,815	41	-	28,223
Other financial assets	-	-	-	1,120	-	1,120
Total financial assets, gross	**34,771**	**145,546**	**38,563**	**6,815**	**-**	**225,695**
Less: impairment allowance	-	-	-	-	-	-
Total financial assets, net	**34,771**	**145,546**	**38,563**	**6,815**	**-**	**225,695**

32 Currency risk

Currency risk exposure

The Bank's currency analysis of financial assets and financial liabilities by currency profile as at 31 December 2018 was as follows:

EUR'000	USD	EUR	RUB	GBP	Other currencies	Total
Financial assets						
Cash and demand deposits with Central banks	23	13,538	2	3	-	13,566
Due from financial institutions	17,504	5,987	9,636	50	21	33,198
Loans and advances due from customers	-	4	-	-	-	4
Financial assets at fair value through other comprehensive income	8,486	25,181	-	-	-	33,667
Other financial assets	201	28	3	-	-	232
Total	**26,214**	**44,738**	**9,641**	**53**	**21**	**80,667**
Financial liabilities						
Deposits and balances due to financial institutions	1	-	-	-	-	1
Current accounts and deposits due to customers	25,714	8,674	10,132	93	18	44,631
Other financial liabilities	-	7	-	5	-	12
Total	**25,715**	**8,681**	**10,132**	**98**	**18**	**44,644**
Net position - on and off statement of financial position	**499**	**36,057**	**8(491)**	**(45)**	**3**	
Spot transaction receivables	-	-	478	-	-	478
Spot transaction liabilities	(476)	-	-	-	-	(476)
Net open position	**23**	**36,057**	**(13)**	**45**	**3**	

NOTES TO THE FINANCIAL STATEMENTS

32 Currency risk, continued

The Bank's currency analysis of financial assets and financial liabilities by currency profile as at 31 December 2017 was as follows:

EUR'000	USD	EUR	RUB	GBP	Other currencies	Total
Financial assets						
Cash and demand deposits with the Central banks	31	73,686	5	3	1	73,724
Due from financial institutions	110,947	10,137	1,046	23	467	122,620
Loans and advances due from customers	-	7	-	-	1	8
Available-for-sale assets	28,182	41	-	-	-	28,223
Other financial assets	633	419	67	-	-	1,120
Total	**139,793**	**84,290**	**1,118**	**26**	**469**	**225,695**
Financial liabilities						
Deposits and balances due to financial institutions	25	3,116	-	-	50	3,191
Current accounts and deposits due to customers	132,737	45,679	7,438	2	465	186,321
Other financial liabilities	118	84	36	-	-	238
Total	**132,880**	**48,879**	**7,474**	**2**	**515**	**189,750**
Net position - on and off statement of financial position	**6,913**	**35,411**	**8 (6,356)**	**24**	**(47)**	
Spot transaction receivables	575	1,101	6,442	-	28	8,147
Spot transaction liabilities	(7,457)	(604)	(101)	-	-	(8,162)
Net open position	**31**	**35,909**	**(15)**	**-**	**(19)**	

Sensitivity analysis

The scenario used for the analysis is based on reasonable volatility of exchange rates equal for all exposures of the Bank in foreign currencies assuming that all other variables, in particular interest rates, remain constant. The analysis is performed on the same basis for both years.

13% of the RUB (2017:13%) and a 5% strengthening of the USD and other foreign currencies against the euro as at 31 December 2018 and 31 December 2017 respectively would have increased profit by the amounts shown below:

	2018 EUR'000	2017 EUR'000
RUB	(2)	(2)
USD	1	2
Other currencies	(2)	(1)
Total	**(3)**	**(1)**

13% of the RUB (2017:13%) and 5% strengthening of the USD and other foreign currencies against the euro as at 31 December 2018 and 31 December 2017 respectively would have had equal absolute value but opposite effect on the above currencies, i.e. decreased profit by the amounts shown above.

NOTES TO THE FINANCIAL STATEMENTS

33 Liquidity risk

Maturity analysis

The table below reflects the maturity analysis of the Bank's financial assets and financial liabilities based on the term from the reporting date until the maturity dates of the respective assets and liabilities. The maturity analysis of the Bank's financial items of financial position and contingent liabilities and commitments as at 31 December 2018 was as follows:

EUR'000	On demand	Up to 1 month	From 1 to 3 months	From 3 to 6 months	From 6 to 12 months	From 1 to 5 years	Longer than 5 years	No maturity	Total
Financial assets									
Cash and demand deposits with the central banks	13,566	-	-	-	-	-	-	-	13,566
Due from financial institutions	7,309	25,889	-	-	-	-	-	-	33,198
Loans and advances due from customers	-	1	-	-	2	1	-	-	4
Financial assets at fair value through other comprehensive income	33,605	-	-	-	-	-	62	-	33,667
Other financial assets	-	56	-	-	-	-	-	176	232
Total	**54,480**	**25,946**	**-**	**-**	**2**	**1**	**62**	**176**	**80,667**
Financial liabilities									
Deposits and balances due to financial institutions	1	-	-	-	-	-	-	-	1
Current accounts and deposits due to customers	42,680	-	-	1,491	100	346	-	14	44,631
Other financial liabilities	12	-	-	-	-	-	-	-	12
Total	**42,693**	**-**	**-**	**1,491**	**100**	**346**	**-**	**14**	**44,644**
Contingent liabilities and commitments	49	-	-	-	-	-	-	-	49
Net liquidity position	**11,836**	**25,946**	**-**	**(1,491)**	**(98)**	**(345)**	**62**	**162**	

Amounts due from credit institutions repayable, according to contracts, by prior notice of withdrawal are included in the category "On demand". Other financial assets and financial liabilities are disclosed in accordance with their remaining contractual maturities.

NOTES TO THE FINANCIAL STATEMENTS

33 Liquidity risk, continued

The maturity analysis of the Bank's financial items of financial position and contingent liabilities and commitments as at 31 December 2017 was as follows:

EUR'000	On demand	Up to 1 month	From 1 to 3 months	From 3 to 6 months	From 6 to 12 months	From 1 to 5 years	Longer than 5 years	No maturity	Total
Financial assets									
Cash and demand deposits with the Central banks	73,724	-	-	-	-	-	-	-	73,724
Due from financial institutions	94,229	28,353	-	-	-	38	-	-	122,620
Loans and advances due from customers	8	-	-	-	-	-	-	-	8
Available-for-sale assets	28,182	-	-	-	-	-	-	41	28,223
Other financial assets	-	73	-	-	2,259	-	-	1,047	1,120
Total	**196,143**	**28,426**	**-**	**-**	**-**	**38**	**-**	**1,088**	**225,695**
Financial liabilities									
Deposits and balances due to financial institutions	3,191	-	-	-	-	-	-	-	3,191
Current accounts and deposits due to customers	185,700	-	-	471	100	480	29	12	186,792
Other financial liabilities	-	-	-	-	-	-	-	238	238
Total	**188,891**	**-**	**-**	**471**	**100**	**480**	**29**	**250**	**190,221**
Contingent liabilities and commitments	192	-	-	-	-	-	15	-	207
Net liquidity position	**7,444**	**28,426**	**-**	**(471)**	**(100)**	**(442)**	**44**	**838**	

NOTES TO THE FINANCIAL STATEMENTS

33 Liquidity risk, continued

Analysis of financial liabilities' contractual undiscounted cash flows

The tables below presents the cash flows payable by the Bank under contractual financial liabilities, including derivative financial liabilities, by remaining contractual maturities as at the reporting date.

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

The analysis of financial liabilities' contractual undiscounted cash flows of the Bank as at 31 December 2018 was as follows:

EUR'000	Carrying amount	Contractual cash flows	Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Longer than 5 years
Non-derivative financial instruments							
Deposits and balances due to financial institutions	1	(1)	-	-	-	-	-
Current accounts and deposits due to customers	44,631	(44,631)	(42,689)	(3)	(1,908)	(31)	-
Other financial liabilities	12	(12)	(12)	-	-	-	-
Total	**44,644**	**(44,644)**	**(42,701)**	**(3)**	**(1,908)**	**(31)**	**-**

The analysis of financial liabilities' contractual undiscounted cash flows of the Bank as at 31 December 2017 was as follows:

EUR'000	Carrying amount	Contractual cash flows	Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Longer than 5 years
Non-derivative financial instruments							
Deposits and balances due to financial institutions	3,191	(3,191)	-	-	-	-	-
Current accounts and deposits due to customers	186,321	(186,321)	(185,712)	(21)	(181)	(407)	-
Other financial liabilities	238	(238)	(238)	-	-	-	-
Total	**189,750**	**(189,750)**	**(185,950)**	**(21)**	**(181)**	**(407)**	**-**

NOTES TO THE FINANCIAL STATEMENTS

34 Interest rate risk

Exposure to interest rate risk

The Bank's exposure to interest rate risk is characterised by the maturity of financial assets and financial liabilities subject to interest rate risk based on the shorter of the remaining maturity dates of financial instruments subject to interest rate risk and the interest rate review dates.

The repricing maturity analysis of financial assets and financial liabilities for the Bank as at 31 December 2018 was as follows:

EUR'000	Up to 1 month	From 1 to 3 months	From 3 to 6 months	From 6 to 12 months	From 1 to 5 years	Longer than 5 years	Interest free	Total
Financial assets								
Cash and demand deposits with the Central banks	13,480	-	-	-	-	-	86	13,566
Due from financial institutions	26,381	-	-	-	-	-	6,817	33,198
Loans and advances due from customers	-	1	-	2	1	-	-	4
Financial assets at fair value through other comprehensive income	322	1,780	6,977	3	24,523	-	62	33,667
Other financial assets	177	-	-	-	-	-	55	232
Total	**40,360**	**1,781**	**6,977**	**5**	**24,524**	**-**	**7,020**	**80,667**
Financial liabilities								
Deposits and balances due to financial institutions	-	-	-	-	-	-	1	1
Current accounts and deposits due to customers	15,925	3	1,488	112	26	-	27,077	44,631
Other financial liabilities	-	-	-	-	-	-	12	12
Total	**15,925**	**3**	**1,488**	**112**	**26**	**-**	**27,090**	**44,644**
Interest rate risk	**24,435**	**1,778**	**5,489**	**(107)**	**24,498**	**-**	**(20,070)**	

NOTES TO THE FINANCIAL STATEMENTS

34 Interest rate risk, continued

The repricing maturity analysis of financial assets and financial liabilities for the Bank as at 31 December 2017 was as follows:

EUR'000	Up to 1 month	From 1 to 3 months	From 3 to 6 months	From 6 to 12 months	From 1 to 5 years	Longer than 5 years	Interest free	Total
Financial assets								
Cash and demand deposits with the Central banks	73,590	-	-	-	-	-	134	73,724
Due from financial institutions	84,892	-	-	38	-	-	37,690	122,620
Loans and advances due from customers	-	-	2	-	6	-	-	8
Available-for-sale assets	170	91	10,571	9,022	8,368	-	-	28,223
Other financial assets	168	-	-	-	-	-	952	1,120
Total	**158,820**	**91**	**10,573**	**9,060**	**8,375**	**-**	**38,776**	**225,695**
Financial liabilities								
Deposits and balances due to financial institutions	-	-	-	-	-	-	3,191	3,191
Current accounts and deposits due to customers	9,626	21	32	149	105	-	176,388	186,321
Other financial liabilities	-	-	-	-	-	-	1,094	1,094
Total	**9,626**	**21**	**32**	**149**	**105**	**-**	**180,673**	**190,606**
Interest rate risk	**149,194**	**70**	**10,541**	**8,911**	**8,270**	**2,024**	**(141,897)**	

NOTES TO THE FINANCIAL STATEMENTS

34 Interest rate risk, continued

Average weighted effective interest rates

The table below shows the Bank's interest rate sensitive assets and liabilities as at 31 December 2018 and 2017 and the corresponding average weighted effective interest rates in 2018 and 2017.

	Carrying amount 31.12.2018 EUR'000	2018 average weighted effective interest rate	Carrying amount 31.12.2017 EUR'000	2017 average weighted effective interest rate
Interest rate sensitive assets				
Due from financial institutions	26,381	0.46%	158,520	0.58%
Financial assets at fair value through other comprehensive income/Available-for-sale assets	33,667	1,75%	28,223	5.65%
Loans and advances due from customers	4	1,18%	8	3.76%
Total	**60,052**		**186,751**	
Interest rate sensitive liabilities				
Deposits and balances due to financial institutions	1	0.29%	3,191	0.28%
Current accounts and deposits due to customers	17,554	0.13%	9,933	0.18%
Total	**17,555**		**13,124**	

Sensitivity analysis

The following table demonstrates the sensitivity to reasonably possible changes in interest rates of the Bank's net interest income. The analysis assumes that all other variables remain constant.

The sensitivity of net interest income is the effect of the assumed changes in interest rates on net interest income for one year following the reporting date, based on the interest rate sensitive non-trading financial assets and financial liabilities held as at 31 December 2018 and 2017.

	Increase in basis points	Sensitivity of net interest income EUR'000	Decrease in basis points	Sensitivity of net interest income EUR'000
As at 31 December 2018				
	+100	1,112	-100	(1,112)
Total effect		**1,112**		**(1,112)**
As at 31 December 2017				
	+100	4,224	-100	(4,224)
Total effect		**4,224**		**(4,224)**

NOTES TO THE FINANCIAL STATEMENTS

34 Interest rate risk, continued

To assess risks in securities portfolio Bank uses Value at Risk (Value-at-Risk) calculation to estimate maximal loss due to prices change. Bank defines Value at Risk (VaR) as possible adverse loss that will not be exceeded with a 99% confidence level, over period 1 day.

	31.12.2018	
	Held for trading instruments	**Financial assets at fair value through other comprehensive income**
Value of portfolio (000' EUR)	-	33,597
1 day VaR (000' EUR)	-	43

35 Events subsequent to the reporting date

No significant subsequent events have occurred in the period from the year-end to the date of these financial statements that would need to be disclosed in these consolidated and separate financial statements, or would require adjustments to be made to these consolidated and separate financial statements and disclosures added to the notes thereto.

***