

**Deloitte &
Touche**



Rietumu Bank

*Independent Auditors' Report and
International Financial Statements
31 December 1996*

**Deloitte Touche
Tohmatsu
International**

**RIETUMU BANK
INDEPENDENT AUDITORS' REPORT AND
INTERNATIONAL FINANCIAL STATEMENTS
YEAR ENDED 31 DECEMBER 1996
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INDEPENDENT AUDITORS' REPORT

To the shareholders of Rietumu Bank:

We have audited the accompanying balance sheet of Rietumu Bank ("the Bank") as of 31 December 1996, and the related profit and loss account and statements of cash flows and shareholders' investment for the year then ended on pages 4 to 7. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion the financial statements referred to above present fairly, in all material respects, the financial position of the Bank as of 31 December 1996, and the results of its operations and its cash flows for the year then ended in accordance with International Accounting Standards.

Deloitte & Touche

Riga, Latvia


20 March 1997

RIETUMU BANK
PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDED 31 DECEMBER 1996

	Notes	1996 LVL'000	1995 LVL'000
Interest income	2	3,369	1,175
Interest expense	3	157	411
NET INTEREST INCOME		3,212	764
Fees and commission income, net	4	2,137	1,791
Foreign exchange profit, net		2,501	2,038
Brokerage, net		692	39
Other operating income	5	36	49
Net gain / (loss) arising from investment activities	6	71	(438)
TOTAL INCOME		8,649	4,243
Provisions	7, 13	685	607
NET INCOME AFTER PROVISIONS		7,964	3,636
Salaries and related social expenses	8	1,095	374
Depreciation	17	157	168
Other administrative expenses	9	1,779	986
PROFIT BEFORE TAXATION		4,933	2,108
Taxation	10	357	2
PROFIT AFTER TAXATION		4,576	2,106

The accompanying accounting policies and notes on pages 8 to 27 are an integral part of these financial statements.

The financial statements on pages 4 to 27 were approved by the Management Board on 20 March 1997 and signed on its behalf by:



 Chairman of the Management Board



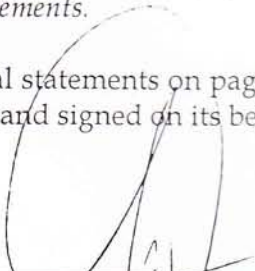
 Chairman of the Supervisory Council

**RIETUMU BANK
BALANCE SHEET
AS AT 31 DECEMBER 1996**


	Notes	1996 LVL'000	1995 LVL'000
ASSETS			
Cash and balances due from the Bank of Latvia	11	11,009	5,095
Due from other banks	12	35,541	37,865
Loans and advances to customers	7, 13	7,491	814
Bonds and other fixed income securities	14	31,861	22
Equity shares and other non-fixed income investments	15	443	176
Investments in affiliates	16	45	165
Fixed assets, net	17	1,130	947
Accrued income and prepayments	18	439	38
Other assets	19	264	221
Total assets		<u><u>88,223</u></u>	<u><u>45,343</u></u>
LIABILITIES			
Due to other banks	20	1,738	1,877
Customer accounts	21	76,820	38,775
Accounts payable and accrued liabilities	22	451	90
Other liabilities	23	88	51
Total liabilities		<u><u>79,097</u></u>	<u><u>40,793</u></u>
SHAREHOLDERS' INVESTMENT			
Share capital	24	4,535	2,500
Legal reserve		15	15
Retained earnings		4,576	2,035
Total shareholders' investment		<u><u>9,126</u></u>	<u><u>4,550</u></u>
Total liabilities and shareholders' investment		<u><u>88,223</u></u>	<u><u>45,343</u></u>
OFF BALANCE SHEET LIABILITIES	25	<u><u>1,444</u></u>	<u><u>256</u></u>

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 Chairman of the Management Board



 Chairman of the Supervisory Council

RIETUMU BANK
STATEMENT OF SHAREHOLDERS' INVESTMENT
AS AT 31 DECEMBER 1996

	Share Capital	Legal Reserve	Retained Earnings / (Accu- mulated Deficit)	Total
	<u>LVL'000</u>	<u>LVL'000</u>	<u>LVL'000</u>	<u>LVL'000</u>
At 31 December 1994	2,500	15	(71)	2,444
Profit for the period	-	-	2,106	2,106
At 31 December 1995	<u>2,500</u>	<u>15</u>	<u>2,035</u>	<u>4,550</u>
Share dividend (Note 24)	2,035	-	(2,035)	-
Profit for the period	<u> </u>	<u> </u>	<u>4,576</u>	<u>4,576</u>
At 31 December 1996	<u><u>4,535</u></u>	<u><u>15</u></u>	<u><u>4,576</u></u>	<u><u>9,126</u></u>

The accompanying accounting policies and notes on pages 8 to 27 are an integral part of these financial statements.

RIETUMU BANK
CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 1996

	1996 LVL'000	1995 LVL'000
CASH FLOWS FROM OPERATING ACTIVITIES		
Profit before taxation	4,933	2,108
Depreciation	157	168
Provisions	685	607
(Recovery)/ Loss on equity shares and other non-fixed income investments	(205)	372
Loss from sale of investment in subsidiary	-	66
Loss on investments in affiliates	134	-
Loss from disposal of fixed assets	3	-
(Increase)/ Decrease in accrued income and prepayments	(401)	15
(Increase)/ Decrease in other assets	(43)	753
Increase in accounts payable and accrued liabilities	361	59
Increase in other liabilities	37	37
Operating profit before changes in operating assets	<u>5,661</u>	<u>4,185</u>
<i>(Increase)/ Decrease in operating assets:</i>		
(Increase)/ Decrease in loans and advances to customers	(7,362)	965
<i>Increase in operating liabilities:</i>		
Increase in customer accounts	38,045	19,760
Decrease in due to other banks	(139)	(1,065)
Net cash from operating activities before tax	<u>36,205</u>	<u>23,845</u>
Taxation	(357)	(2)
Net cash and cash equivalents from operating activities	<u>35,848</u>	<u>23,843</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Increase in bonds and other fixed income securities	(31,839)	(22)
(Increase)/ Decrease in equity shares and other non-fixed income investments	(62)	75
Increase in investments in affiliates	(14)	(30)
Purchase of fixed assets	(343)	(817)
Net cash and cash equivalents used in investing activities	<u>(32,258)</u>	<u>(794)</u>
Net increase in cash and cash equivalents	3,590	23,049
Cash and cash equivalents at beginning of year	<u>42,960</u>	<u>19,911</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u><u>46,550</u></u>	<u><u>42,960</u></u>

The accompanying accounting policies and notes on pages 8 to 27 are an integral part of these financial statements.

**RIETUMU BANK
ACCOUNTING POLICIES
31 DECEMBER 1996**

The significant accounting policies adopted by Rietumu Bank ("The Bank") are set out below.

BASIS OF PREPARATION

The financial statements presented include only the accounts of the Bank.

The financial statements have been prepared on the historical cost basis of accounting, in accordance with International Accounting Standards (IAS) and general practices within the banking industry. The following summarises the more significant of these policies.

The accompanying financial statements are presented in the national currency of Latvia, the Lats ("LVL").

CASH AND CASH EQUIVALENTS

For the purposes of the statements of cash flows, the Bank considers cash and due from banks as cash and cash equivalents.

INTEREST, FEES AND COMMISSIONS

Interest income is recognised on the accrual basis. The Bank does not accrue for interest on loans it classifies as other than standard. For loans other than standard all interest income accrued is reversed and no further accruals are made until the arrears are received.

Commissions, fees and other income are credited to income when earned.

Interest expense is recognised on the accrual basis.

Commission, fees, and other expenses are debited to expense when incurred.

FOREIGN CURRENCIES

Transactions denominated in foreign currency are translated into LVL at the official Bank of Latvia exchange rate on the date of the transaction, which approximates the prevailing market rates. Monetary assets and liabilities, including unmatured commitments to deliver or acquire foreign currencies under spot exchange transactions, if any, are translated at the rate of exchange on the balance sheet date. The applicable rates used for the principal currencies as at 31 December were as follows:

	<u>1996</u>	<u>1995</u>
USD	0.556	0.537
DEM	0.358	0.376
RUR	0.0001002	0.0001164

RIETUMU BANK
ACCOUNTING POLICIES
31 DECEMBER 1996

All resulting gains and losses relating to cash are recorded in the profit and loss account in the period in which they arise. Gains and losses on translation are credited or charged at foreign exchange rates prevailing at year end. Due to Latvian accounting practices it is not practical to distinguish between gains and losses on trading activities and gains and losses on translation of foreign currency assets and liabilities.

PROVISION FOR LOAN LOSSES

As at 31 December 1995 and 1996, loans represent the unpaid principal balance of loans less provision for loan losses.

The Bank provides commercial and consumer loans to customers throughout its market area. The economic condition of the market area may have an impact on the borrower's ability to repay their loans. Management and the Directors have considered risk in determining the balance of provisions and possible loan losses. Provision for loan losses as at the balance sheet date are established in accordance with IAS and represent the estimated amounts of probable losses that have been incurred at the balance sheet date. The value of the collateral held in connection with the loan is based on its estimated realisable value and is taken into account when estimating the required provision.

The provision for loan losses is composed of estimated figures for the following:

- specific provision for loans identified as non-performing
- specific provision for probable losses on credits identified as high risk
- general provision for the Bank's total exposure to:
 - identified loan concentration risk
 - each customer and their general financial position
 - collateral values
 - possible measures implemented to improve troubled customers' financial position
 - general market or operating events that have occurred or have yet to occur, prior or subsequent to the balance sheet date, for which a specific provision is not yet quantifiable.

The level of the provision is based on estimates considering known relevant factors affecting loan collectibility and collateral values. Ultimate losses may vary from the current estimates. These estimates are reviewed periodically, and as adjustments become necessary, they are reported in earnings in the period in which they become known. Due to an inherent lack of reliable information about the customer's financial position, the estimate of probable losses is uncertain. Nevertheless, management and the Directors have made their best estimates of losses and believe those loss estimates presented in the financial statements are reasonable in light of available information and do not vary materially from the guidelines established by the Bank of Latvia regarding provision for loan losses.

**RIETUMU BANK
ACCOUNTING POLICIES
31 DECEMBER 1996**

INVESTMENTS

Debt securities and equity shares are held both for investment purposes, where intended for use on a continuing basis in the activities of the Bank, and as part of a trading portfolio.

Debt securities held are shown at their maturity value plus any unamortised premium or less any unamortised discount on their purchase. Premiums and discounts are amortised on a systematic basis to maturity and taken to the profit and loss account. All other securities are shown at cost, less any provision for permanent diminution in value.

INVESTMENTS IN AFFILIATES

Investments in subsidiaries and associates are stated at cost. Financial statements which consolidate the financial statements of the Bank and its subsidiaries have not been prepared as the financial effects are not considered to be significant.

TANGIBLE FIXED ASSETS

Tangible fixed assets are stated at historical cost, less accumulated depreciation. If the fair value of a fixed asset is lower than its carrying amount, due to circumstances not considered to be temporary, the fixed asset is written down to its fair market value.

Depreciation is provided in equal monthly instalments, except for the month placed in service, over the expected useful lives as follows:

Vehicles	5 years
Furniture, fixtures and equipment	10 years
Computer hardware and software	5 years
Leasehold refurbishments	10 years
Other	2 to 5 years

All assets in excess of LVL 50 are capitalised. Gains and losses on disposal of fixed assets are recognised in the profit and loss account in the year of disposal.

FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISK

In the normal course of business, the Bank enters into financial instruments with off-balance sheet risk, which include foreign exchange contracts and issued guarantees. These financial instruments involve, to varying degrees, elements of credit, interest rate and currency risk. Provision is made for estimated losses, if any, on such off-balance sheet items.

REGULATORY REQUIREMENTS

The Bank is subject to the regulatory requirements of the Bank of Latvia. These requirements include capital adequacy, liquidity, foreign currency position, and loan concentration for individual loan customers.