BANKING OPERATION

GENERAL INFORMATION

In 2009, two branches of Member State banks were registered with the Commercial Register of the Republic of Latvia, i.e. *Pohjola Bank Plc* Latvia branch at the beginning of the year and the branch of the joint stock company *SNORAS* in 3Q, however, both branches are planning to commence their financial activities in 2010. At end-2009 there were still 21 banks and six branches of foreign banks operating in the Republic of Latvia.

In the reporting year, AS "Akciju komercbanka "Baltikums"" branch commenced its activities in Cyprus (Limassol), whereas AS DnB NORD Banka Estonia branch ceased its activities. Thus the number branches of Latvian banks operating in Member States remained unchanged – 10.

By 31 December 2009, licences from the financial sector supervisory authorities of the European Economic Area regarding the intention to undertake financial services in Member States without opening a branch were issued to the state AS "Latvijas Hipotēku un zemes banka" and AS "NORVIK BANKA" (in Lithuania and Estonia), AS "Akciju komercbanka "Baltikums"" (in Lithuania, Estonia and Cyprus), AS "Rietumu Banka" (in the United Kingdom, Ireland and Germany), AS "SEB banka" (in Ireland and Lithuania), AS "Parex banka" (in Denmark, Italy, Norway and Finland) and AS "Baltic International Bank" (in the United Kingdom).

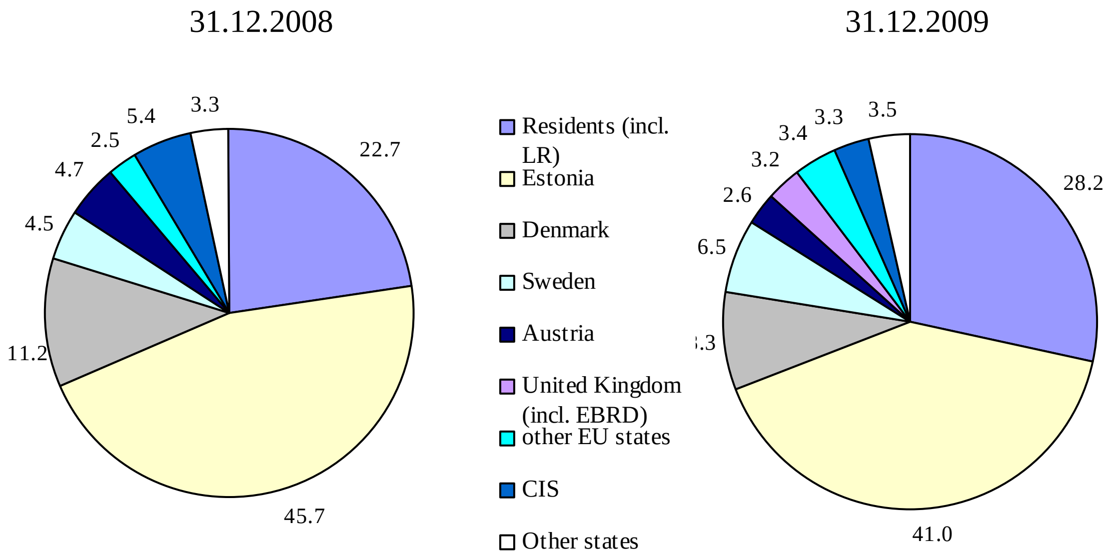
Changes in the names of several banks and branches of the Member State banks took place in 2009. AS "Hansabanka" accomplished the process of the change of brand that was launched in the autumn of 2008 and as of 17 March 2009 changed its name to "Swedbank" AS. Also, the branch of "Balti Investeeringute Grupi Pank AS" registered the change of name with the Commercial Register of the Republic of Latvia, and as from 27 March 2009 it is the Latvian branch of *BIGBANK AS* and joint stock company "Latvijas Tirdzniecības banka" – registered as AS LTB Bank as from 24 April 2009.

In the reporting year, banks continued strengthening their capital base, increasing both their share capital (AS "Akciju komercbanka "Baltikums"", AS "Baltic International Bank", AS DnB NORD Banka, AS "GE Money Bank", AS "Latvijas Krājbanka", AS "NORVIK BANKA", AS "Parex banka", AS "PrivatBank", AS "Rietumu Banka", AS "SEB banka", "Swedbank" AS, VAS "Latvijas Hipotēku un zemes banka" and AS "VEF banka") and subordinated capital (AS DnB NORD Banka, AS "Latvijas Krājbanka", AS "Parex banka", AS "SEB banka", "Swedbank" AS, AS "PrivatBank" and AS "VEF banka"), as well as reserve capital (AS DnB NORD Banka and AS "Rietumu Banka"). Total bank paid-up share capital in 2009 grew by 82% and at end of the year accounted for 1,616.9 million lats, including the share of foreign capital amounting to 71.8% (compared to 77.3% on 31 December 2008) (see Figure 1).

Figure 1

BANKING PAID-UP SHARE CAPITAL BROKEN BY COUNTRIES

(at end-period; as a percentage)



Following the increasing of share capital of the state-owned AS "Latvijas Hipotēku un zemes banka" and AS "Parex banka" in 2009, also the state-owned share in total paid-up banking share capital grew and by end of the year totalled 18% (compared to 11.7% on 31 December 2008).

By end-2009, 10 banks operated as subsidiaries of Member State and foreign banks, and the market share of those banks constituted 55% of total banking sector assets on 31 December, including five subsidiaries of Member States banks – 51.4%, whereas five CIS[1] subsidiaries – 3.6% (compared to 54.2%, 50.6% and 3.6% on 31 December 2008, respectively). By the end of the year, the market share of six branches of Member States banks in total assets made up 12% (compared to 11.5% on 31 December 2008).

MARKET CONCENTRATION

Herfindhal–Hirschman index (HHI)[2] and determining of the market share of five largest market participants (CR5) are frequently applied methods for the analysis of the level of concentration in a market.

In 2009, the market share of five largest banks contracted both in assets and loans as well as in deposits and at end of the year made up 68.2%, 74.2% and 59.9%, respectively (compared to 69.5%, 74.5% and 63.4% on 31 December 2008) (see Figure 2).

[1] CIS – Commonwealth of Independent States.

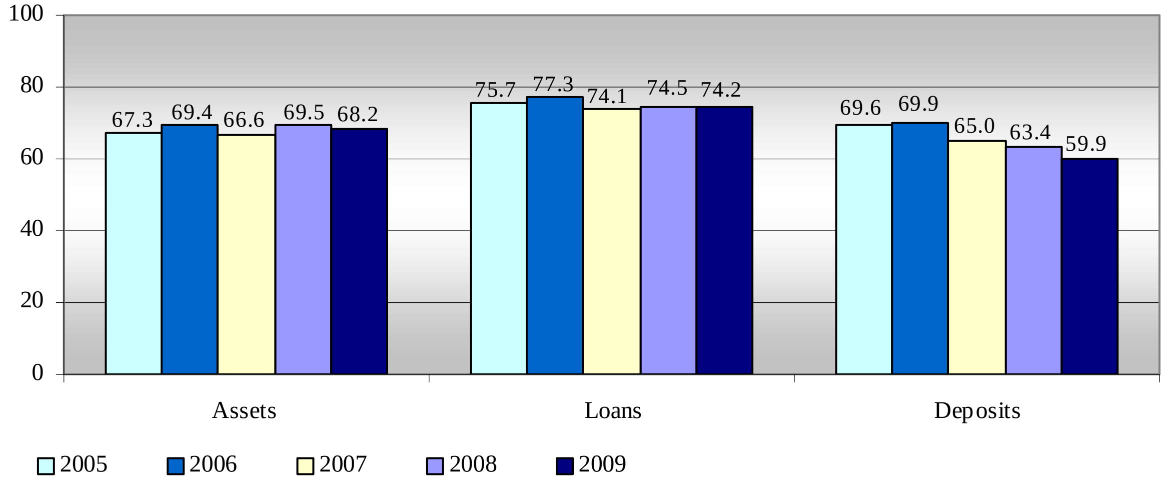
[2] Herfindhal-Hirschman index (HHI) – sum of the squares of the market shares of individual companies.

$$HHI=\sum_{i=1}^{N} MS_i^2$$

N – number of companies; MS – market share of individual companies.

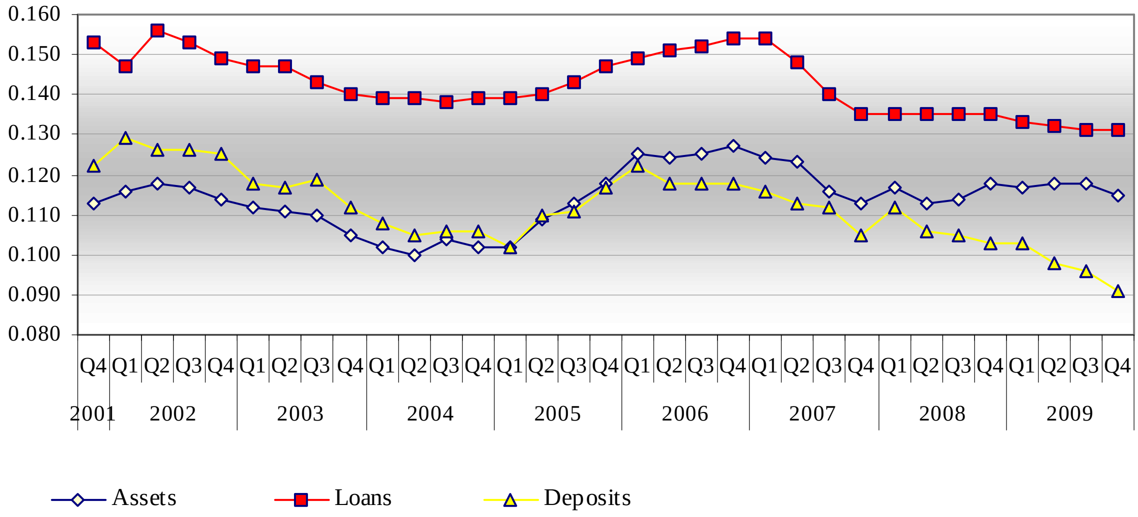
Figure 2

MARKET SHARE OF FIVE LARGEST LATVIAN BANKS
(at end of period; as a percentage)



In 2009, the HHI index for assets and loans changed insignificantly while a decrease in deposits was notable, totalling 0.115, 0.131 and 0.091, respectively, at end of the year (compared to 0.118, 0.118 and 0.103 on 31 December 2008)[3] (see Figure 3).

Figure 3
HHI INDEX FOR BANKING ASSETS, LOANS AND DEPOSITS
(at end of period)



A gradual decrease in the market share of the largest banks in total deposits furthered a HHI decrease in 2009; this in turn indicates a growing competition in the Latvian banking sector. Sufficiency of banks is an impediment to the predominance of any of banks in the market.

[3] HHI may vary between 0 and 1. The higher HHI, the higher is the level of concentration and the lower is competition in the market, namely, where HHI approaches 1, absolute concentration or monopoly is observed.

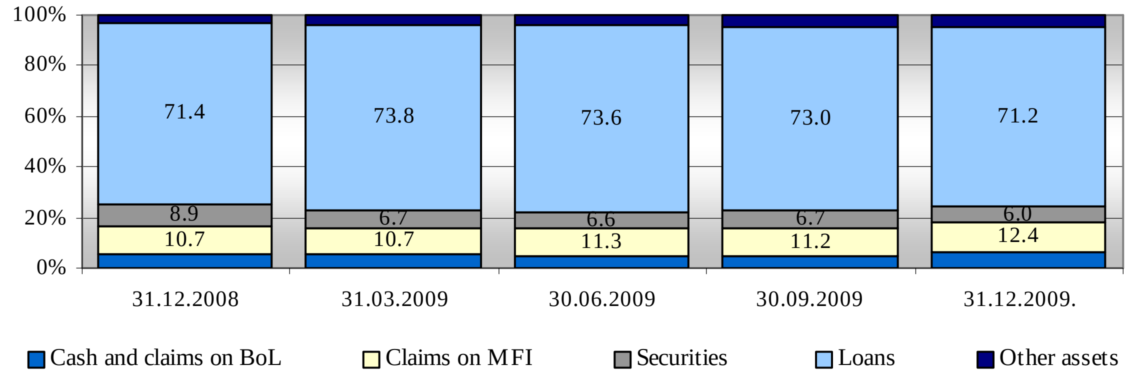
STRUCTURE OF ASSETS AND LIABILITIES

In 2009, the amount of banking sector assets contracted by 1.6 billion lats, or 6.7%, and their amount at the end of December was 21.7 billion lats (in 2008 the amount of assets rose by 1.3 billion lats or by 6.1%). At end-2009, loans constituted the major share in the structure of banking assets, 71.2%, while the share of banking claims on monetary financial institutions (MFI)[4] was 12.4% and investments in securities were 6% (compared to 71.4%, 10.7% and 8.9%, respectively, on 31 December 2008) (see Figure 4).

Figure 4

STRUCTURE OF ASSETS

(as a percentage)

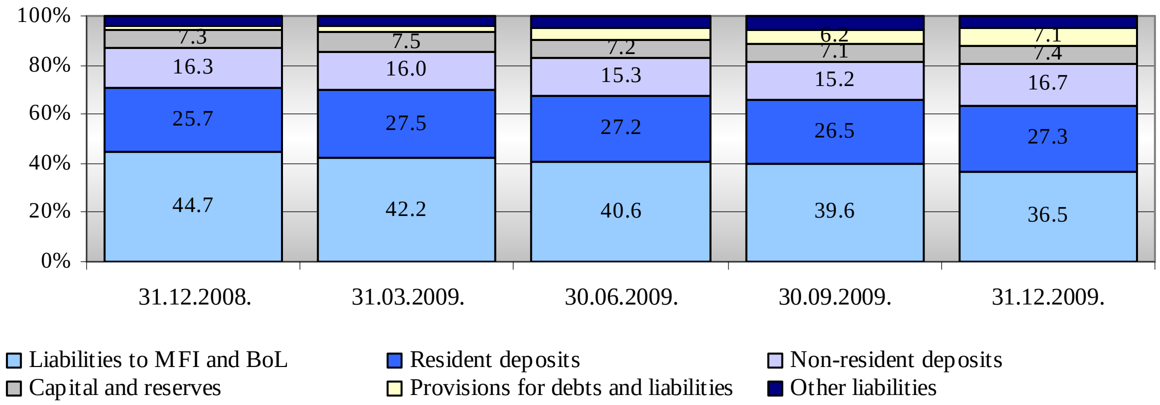


At the end of reporting year, the share of resident deposits in the banking liabilities structure constituted 27.3%, non-resident deposits – 16.7%, while the banking liabilities to MFI and the Bank of Latvia (BoL) – 36.5% (compared to 25.7%, 16.3% and 44.7% on 31 December 2008) (see Figure 5).

Figure 5

STRUCTURE OF LIABILITIES

(as a percentage)



[4] Monetary financial institutions (MFI) – credit institutions and monetary market funds.

In 2009, continuing repayment of syndicated loans (six banks had already repaid their syndicated debts in the amount of 490 million lats) and following a decrease in financing from parent banks, total bank liabilities to MFI shrank by 20.2%. At the end of the reporting year, financing of foreign banks to their subsidiaries and branches in Latvia still constituted the major share – 76.5% % of total banking liabilities to MFI (compared to 73.8% on 31 December 2008). The remaining amount of syndicated loans in the banking sector by the end of the year made up less than 3% of total banking sector's assets (compared to 5% at end-2008).

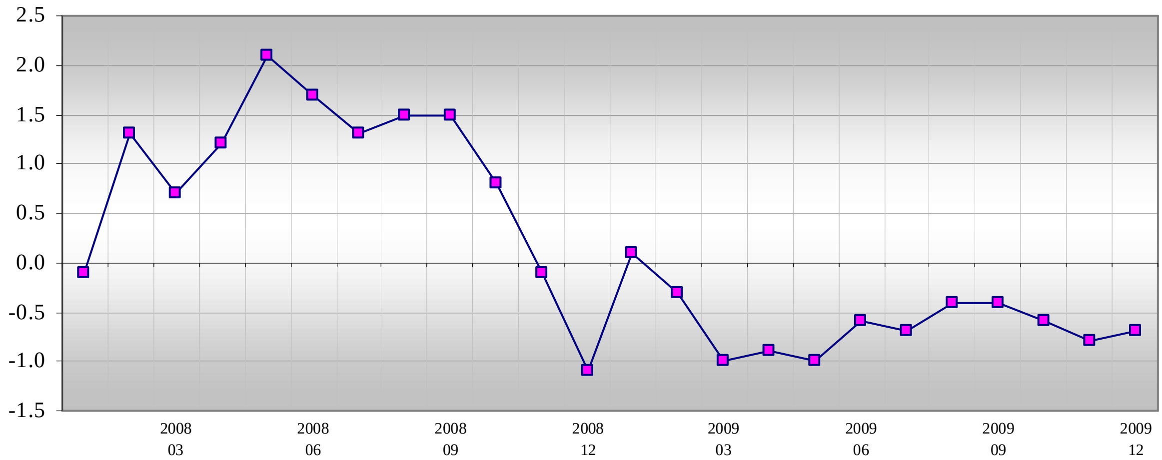
LOANS

In 2009, the balance of total banking loan portfolio started reducing month-on-month by 0.6% on the average as from February, attesting to the banks' prudential lending policy and a significant decrease in loan demand. In total, the loan portfolio of banks shrank by 1.2 billion lats or 7% over the year and by the end of December totalled 15.4 billion lats (in comparison with 2008 when it grew by 1.7 billion lats or 11.2%) (see Figure 6).

Figure 6

LOAN BALANCE MONTHLY GROWTH RATE

(as a percentage)



Loan portfolio broken down by the economic sector

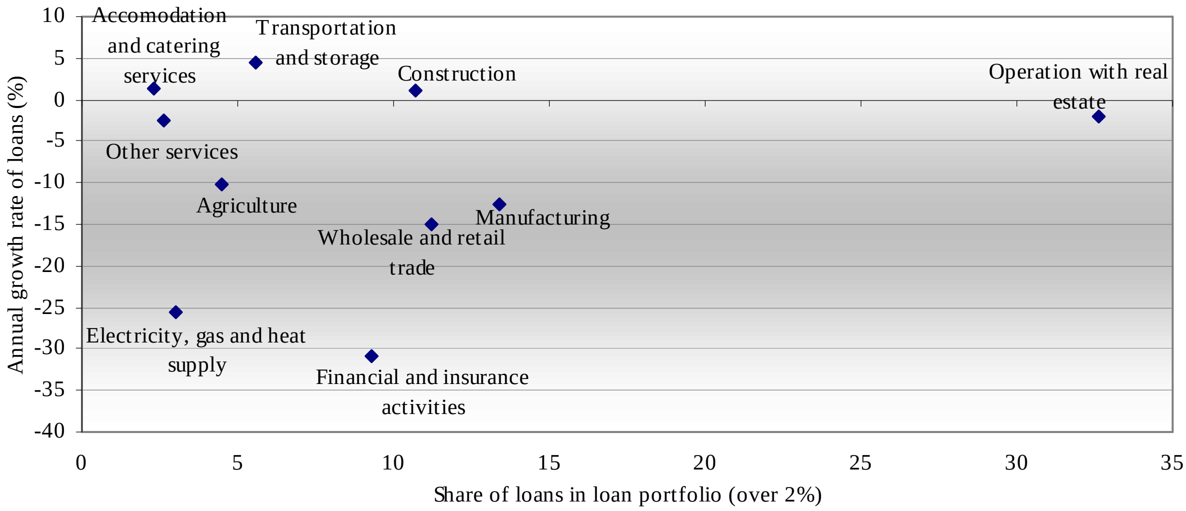
The amount of loans issued to the development of Latvian national economy in the reporting year reduced by 749 million lats or by 9.2% and at end-December totalled 7.4 billion lats (compared to 1.1 billion lats or 15.8% in 2008). In the reporting year, the most significant loan balance decrease was in such economic sectors as financial intermediation and insurance (by 310 million lats or 30.9%), trade (by 147 million lats or 15%), manufacturing industry (by 146 million lats or 12.7%), electricity, gas and heat supply (by 75 million lats or 25.5%) and transactions in real estate (by 50 million lats or 2%). Though total balance of loans granted to the economic development decreased in 2009, the balance of loans issued to several sectors (covering 21.8% of total share in loan portfolio) increased, for instance, transport and storage – by 18 million lats or 4.5%, professional, scientific and technical services – by 13 million lats or 60.8% and construction – by 8 million lats or 1.1%.

Largest amounts of loans were still granted to such national economic sectors as real estate transactions (32.6%), manufacturing industry (13.4%), trade (11.2%) and construction (10.7%) (see Figure 7).

Figure 7

SHARE OF LOANS ISSUED TO NATIONAL ECONOMY SECTORS OF BANKING ASSETS IN CREDIT PORTFOLIO* AND ANNUAL GROWTH RATE OF SUCH LOANS

(31.12.2009; as a percentage)



* Banking loan portfolio comprises loans issued to resident financial institutions, state enterprises and private companies.

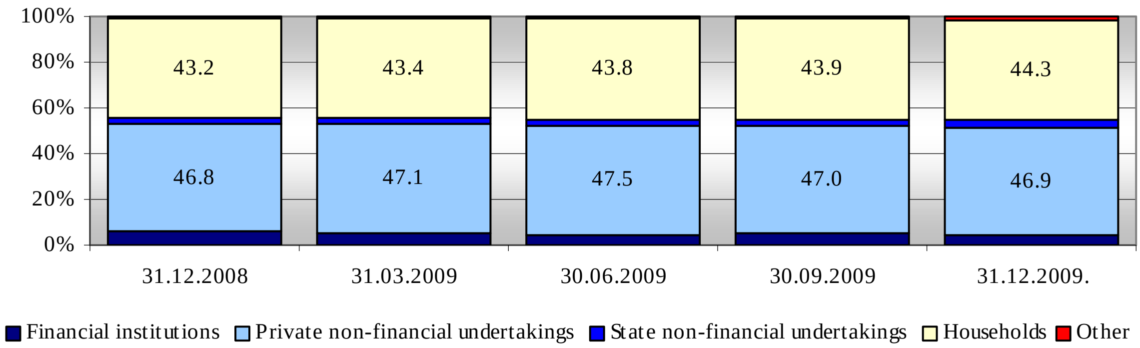
Loan portfolio broken down by borrowers (residents)

By end-2009, of total amount of loans to non-banks, 88.6% were issued to residents, of which private non-financial undertakings – 46.9%, households – 44.3% and financial institutions – 4.6% (compared to 46.8%, 43.2% and 6.1% on 31 December 2008) (see Figure 8). In the reporting year, the most substantial decrease was in the amount of loans issued to private non-financial undertakings - by 491 million lats or 7.1%, to households – by 316 million lats or 5% and financial institutions – by 272 million lats or 30.4%, whereas the balance of loans issued to state non-financial undertakings grew by 14.6 million lats or 3.8%.

Figure 8

BORROWERS BROKEN BY SECTORS

(as a percentage)



In the reporting year, loan balance and the number of loans issued to households for housing acquisition decreased by 226 million lats (or 4.5%) and by 6.7 thousand, as well as consumption loans by 76 million lats (or 9.7%) and by 43.9 thousand, respectively, and payment card loans by 29 million lats (or 9.7%) and by 5.4 thousand. The balance of other loans issued to households rose by 8.8 million lats or 1.8%, but with an increase in their number by 58 thousand also total number of loans granted to households increased and at end-December amounted to 1,210 thousand. Of total number of loans issued to households, the greater part, or 61.7%, was payment card and current account loans, 15.3% were consumption loans, but 12.5% were loans for housing acquisition, reconstruction and repair. Loan balance issued for housing acquisition by end-December totalled 4,826 million lats, while for consumption – 712 million lats, i.e. 79.7% and 11.8%, respectively, of loans issued to households.

In 2009, the average amount of a loan issued to one household did not change significantly and by end-December was as follow: 32 thousand lats for purchase, reconstruction and repair of housing, 2.5 thousand lats for consumption, and 361 lats for payment cards.

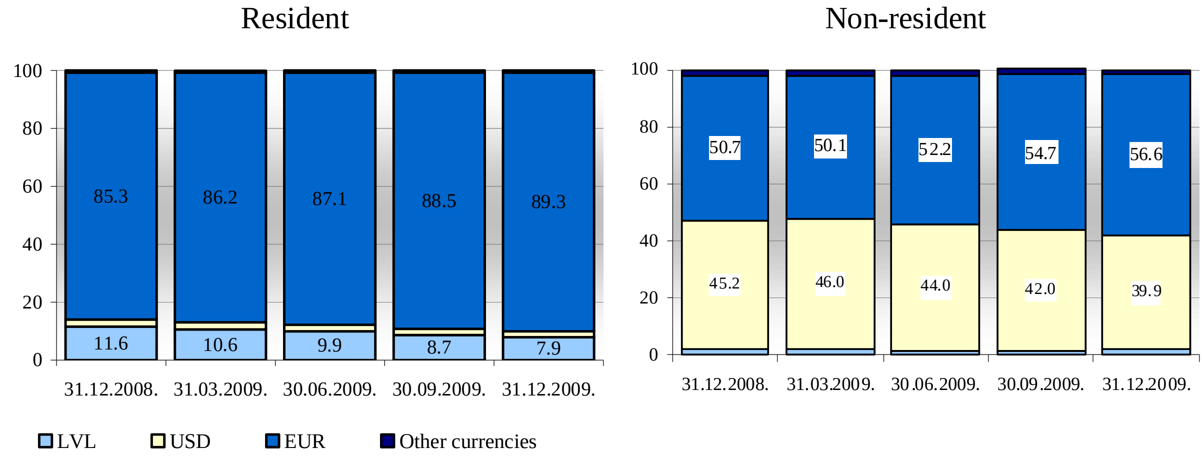
Loan portfolio broken down by currency

In the reporting year, following a decrease in resident loan portfolio, the structure of currencies also changed, namely, upon the steepest decline in loans issued in lats and US dollars (by 37% and 18.3%, respectively), the share of loans issued in euros in the resident loan portfolio at end-December totalled 89.3%, while only 7.9% of loans were issued in lats (85.3% and 11.6% at end-2008). Meanwhile following an increase in the amount of loans in euros by 6.5% in the reporting year, also the share of those loans in non-resident loan portfolio also grew and at end-December amounted to 56.6% (compared to 50.7% at end-2008) (see Figure 9).

Figure 9

LOAN PORTFOLIO BROKEN DOWN BY CURRENCY

(as a percentage)



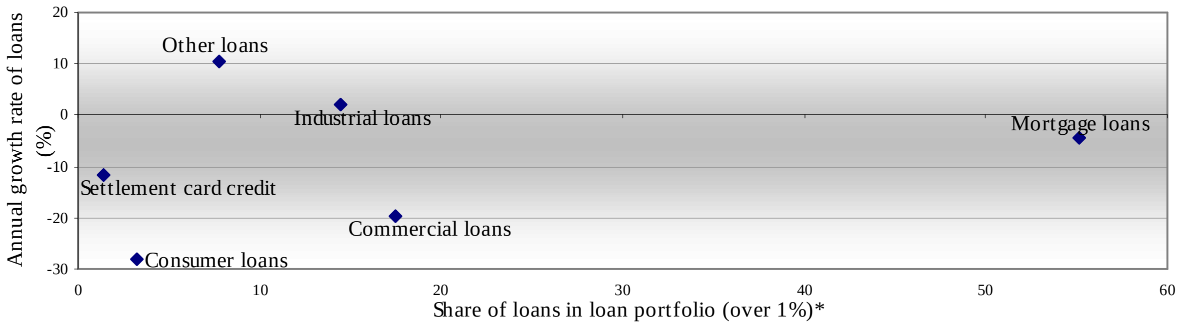
Loan portfolio broken down by loan type

Though in 2009 commercial loans (to increase current assets of enterprises) saw the most notable decrease (by 655 million lats or 19.7%) as well as mortgage loans (by 402 million lats or 4.6%), they still made up the greatest share in the banking total loan portfolio, i.e. 17.5% and 55.1%, respectively (compared to 20.3% and 53.7% at end-2008). Following a year-on-year increase in industrial loans[5] by 2.1%, their share in total banking loan portfolio also grew from 13.2% at end-2008 to14.5% on 31 December 2009 (see Figure 10).

Figure 10

TYPES OF LOANS AND THEIR ANNUAL GROWTH RATE

(31.12.2009; as a percentage)



*Banking loan portfolio comprises loans issued to residents except the loans to central/local governments and transit loans.

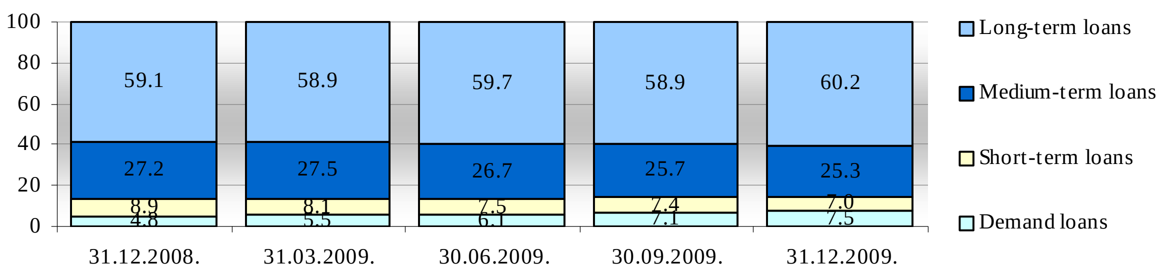
Term structure of loan portfolio

Changes in term structure of banking loan portfolio in the reporting year reflected measures taken by banks for loan restructuring. At end-December, the share of long-term loans (more than 5 years) in banking loan portfolio accounted for 60.2%, medium-term loans (between one and five years), 25.3%, short-term loans (up to one year), 7%, and demand loans, 7.5% (compared to 59.1%, 27.2%, 8.9% and 4.8%, respectively, at end-2008) (see Figure 11).

Figure 11

TERM STRUCTURE OF LOAN PORTFOLIO

(as a percentage)

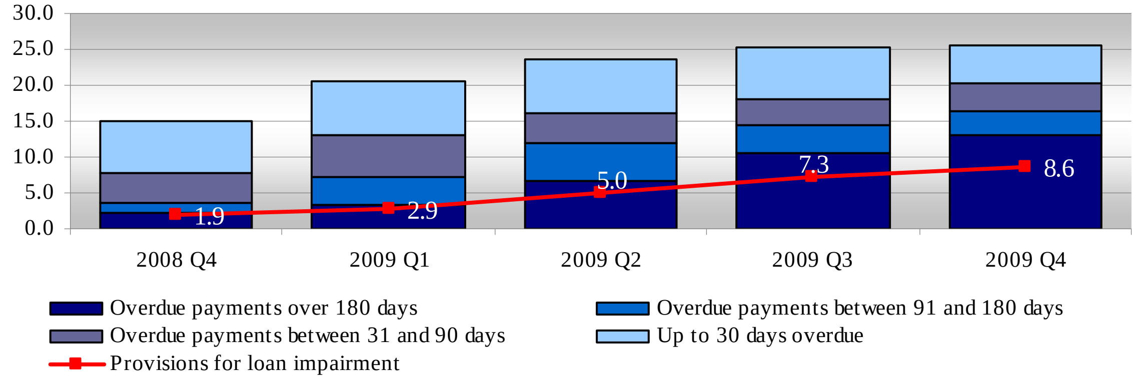


[5] Industrial loans – loans issued to a non-financial undertaking, financial institution or non-profit institution servicing households for the acquisition of fixed assets and financing other long-term investment projects, except the loans recognized as financial leasing or mortgage loan.

Quality of loan portfolio

In 2009 in times of economic downturn, increasing unemployment and spreading economic uncertainty the borrowers' creditworthiness was still declining. The share of loans without delayed payments (principal amount and/or interest payment) in total loans decreased from 85% at end-2008 to 74.5% end of the year, whereas the proportion of borrowers incapable to meet their liabilities for a lengthy period of time grew and the share of loans with payments overdue more than 90 days in the loan portfolio made up 16.4% or 2.5 billion lats (compared to 3.6% at end-2008). Upon deterioration in the loan portfolio quality provisioning for loan principal amount in the reporting year grew by 1 billion lats and at end-December totalled 1,328 million lats. At end-2009, provisioning for loan principal amount made up 8.6% of banking loan portfolio (compared to 1.9% at end-2008) (see Figure 12).

Figure 12
OUTSTANDING LOANS AND PROVISIONS FOR LOAN PRINCIPAL AMOUNT AS PERCENTAGE OF LOAN PORTFOLIO
(at end-period; as a percentage)



At the end of the year, the share of loans with payments overdue above 90 days in the loan balance for 14 banks did not exceed the average banking sector ratio, i.e.16.4%, and the share of those banks' assets in total assets of the banking sector accounted for 41.8% (compared to 99.8% at end-2008) (see Table 1). Whereas the share of loans with payments overdue above 90 days in the loan balances for four banks (constituting 3% in total banking sector assets) was above 25.1%.

Table 1
BREAKDOWN OF BANKS BY PROPORTION OF LOANS WITH PAYMENTS OVERDUE ABOVE 90 DAYS IN BALANCE OF BANK LOAN PORTFOLIO

Share of loans with payments overdue above 90 days in a bank loan portfolio (%)	31.12.2008		31.12.2009	
	Number of banks and branches of foreign banks	Banking market share (% of total banking assets)	Number of banks and branches of foreign banks	Banking market share (% of total banking assets)
Under 10	23	97.1	7	17.0
10–16.4	3	2.7	7	24.8
16.5–25	1	0.2	9	55.2
Above 25.1	-	-	4	3.0

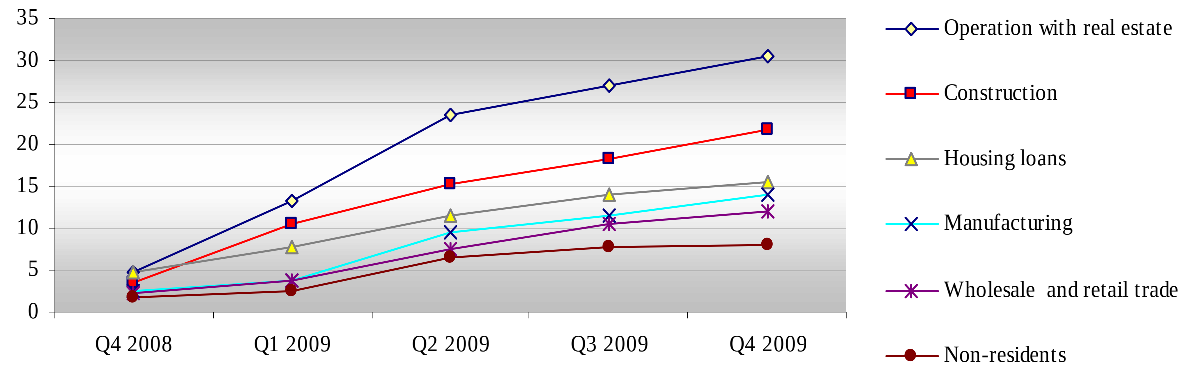
At end-2009, 18.5% of resident corporate loan portfolio and 16.8% of resident household loan portfolio were loans with payments overdue above 90 days, and the number of those outstanding loans was 14.9 thousand and 150.7 thousand, respectively (compared to end-2008 – 10.6 thousand and 84.2 thousand, respectively). Of household loans with payments overdue above 90 days, a majority or 109.7 thousand were payment card loans, consumption loans – 19.8 thousand, loans for the acquisition, reconstruction and repair of housing – 13.4 thousand and others – 7.8 thousand (at end-2008 – 66.7 thousand, 12.2 thousand, 4.4 thousand and 952, respectively).

A steepest increase in loans with payments overdue above 90 days in 2009 was in the real estate sector, i.e. loans granted to real estate transactions and construction enterprises, as well as loans for the acquisition, reconstruction and repair of housing. The share of those outstanding loans in the loan portfolio of each sector at end of the year totalled 30.4%, 21.7% and 15.4% (compared to end-2008 – 4.7%, 3.4% and 4.7%, respectively) (see Figure 13).

Figure 13

SHARE OF LOANS ABOVE 90 DAYS PAST DUE IN LOAN PORTFOLIO OF EACH SECTOR

(as a percentage)

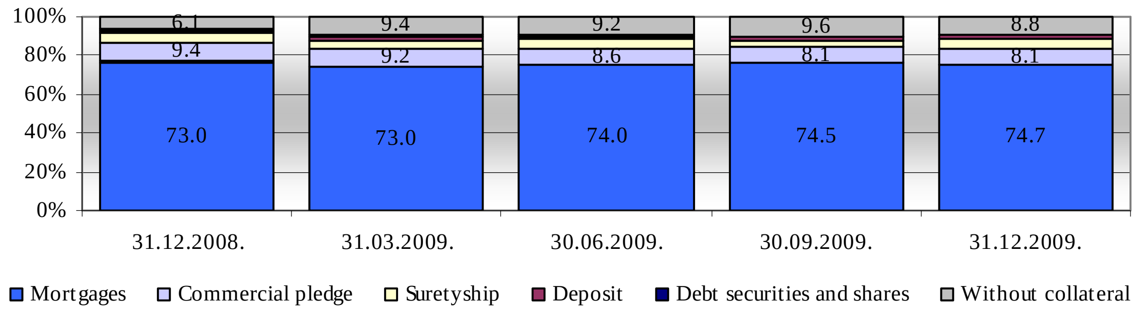


Loan portfolio collateral

At end-2009, of total loans 74.7% were secured by a mortgage[6], of which most popular were housing first mortgages, 34.5%, and commercial property first mortgages, 27% (compared to 73%, 33.2% and 26.4%, respectively, at end-2008). Of other types of loan collateral, most popular still were commercial pledges, 8.1% (compared to 9.4% at end-2008) (see Figure 14).

[6] Mortgage is a pledge of real estate property registered with the Land Register, retaining a mortgager's property rights under restrictions set by a pledge holder. In case of a mortgager's default, the pledged property goes on sale.

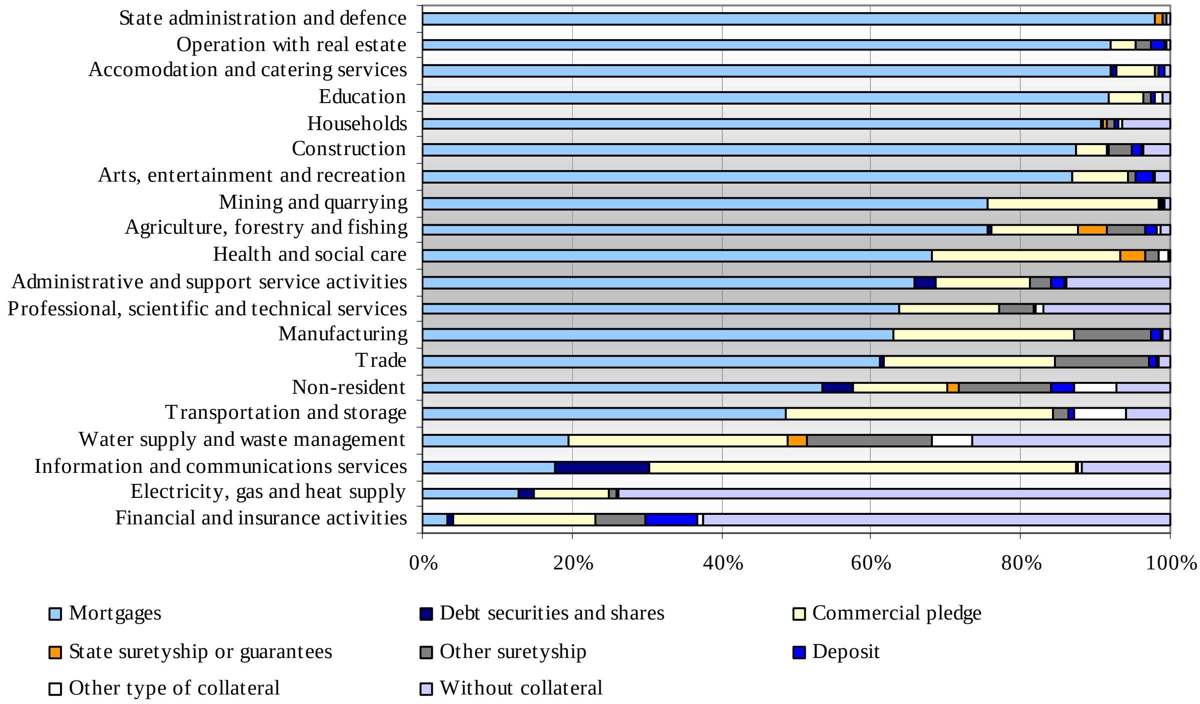
Figure 14
TYPES OF LOAN PORTFOLIO COLLATERAL
(% to the loan balance)



At the end of the reporting year mortgages prevailed as collateral type for loans issued to such sectors as state administration and defence – 97.9%, transactions in real estate – 92%, dwelling and catering services – 91.9%, education – 91.9%, as well as construction – 87.4%. Whereas commercial pledges were popular collateral with such sectors as information and communications services, transport and storage, as well as water supply and waste disposal, which accounted for 57.1%, 35.7% and 29.4%, respectively, of total loans for each sector. Shares and debt securities still were less popular type of loan collateral as well as deposits, which served as collateral for about 2.3% of total loans issued by banks. Of loans to the enterprises (mostly state and local government authorities), which represent electricity, gas and heat supply sectors, at end-December 73.7% were granted without any collateral (i.e. 2.2% of total loans issued to national economy). Of loans secured by state suretyship and guarantee, major part or about 37% were student loans issued to resident households at end-December (see Figure 15).

Of loans issued to households, 90.7% were secured by mortgage; incl. loans for the acquisition, reconstruction and repair of housing were mortgage-backed by 99.6%.

Figure 15
TYPES OF LOAN PORTFOLIO COLLATERAL BROKEN BY ECONOMIC SECTORS
(31.12.2009; as a percentage)

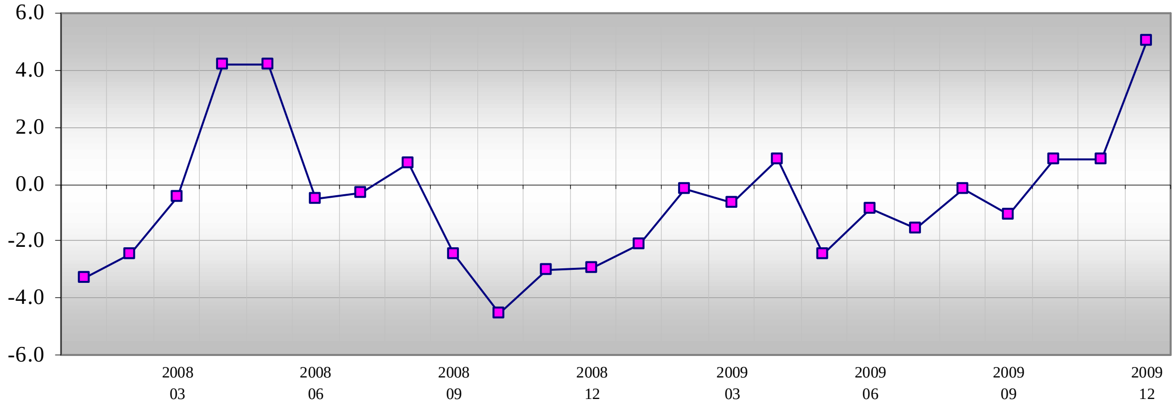


DEPOSITS

In 2009, total volume of deposits in the banking sector (excluding deposits of the State Treasury in AS "Parex banka") contracted by 158 million lats, or 1.7%, of which the amount of resident deposits – by 1 million lats, or 0.02%, whereas the amount of non-resident deposits – by 157 million lats, or 4.2% (compared to decreases by 3.5% and 19.2% in 2008). Though till end-September of 2009 deposits monthly shrank by par 1.1% on the average (except for a 0.8% decrease in April), since October deposit stock in the banking sector began increasing, i.e. in October – by 0.9%, in November – by 0.8% and in December – by 5% (see Figure 16).

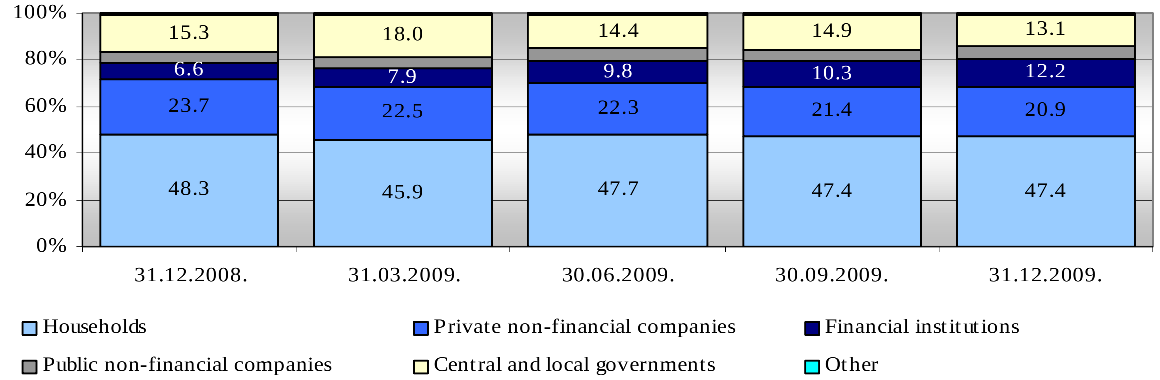
Figure 16

NON-BANK DEPOSIT MONTHLY GROWTH RATE
(excluding deposits of the State Treasury with AS "Parex banka")
(as a percentage)



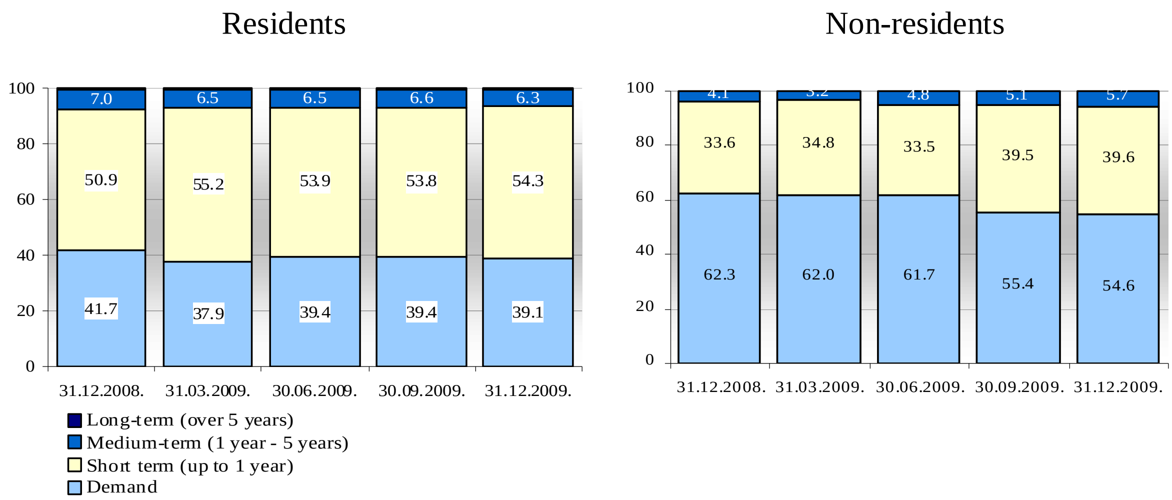
The share of resident deposits in total deposits made up 62% at end-year (compared to 61.2% at end-2008). The greater part of resident deposits was household deposits (47.4%) and private non-financial companies' deposits (20.9%). In 2009, upon a material increase in deposits of resident financial institutions (by 83%), their share also grew in total resident deposits and at the end of the year totalled 12.2% (compared to 6.6% at end-2008) (see Figure 17). Though in 4Q 2009 there was an increase in both private non-financial companies and households deposits, i.e. by 10 million lats and 90 million lats, respectively (or 0.8% and 3.3%, respectively), however, in comparison with December 2008 their share had shrunk by 12.6% and 2.7%, respectively. Deposits of private non-financial undertakings (80.7%) traditionally retained a major share of total non-resident deposits (compared to76.6% at end-2008).

Figure 17
SECTORAL BREAKDOWN OF DEPOSITORS (RESIDENTS)
(as a percentage)



In the reporting year, changes in the deposit term structure still continued. In resident deposits, the share of demand deposit stock, both medium-term and long-term deposits shrank by 2.6, 0.7 and 0.2 percentage points, respectively, while the share of short-term deposits grew by 3.4 percentage points. Whereas in non-resident deposits, only the amount of demand deposits contracted (by 7.7 percentage points), while term deposits grew, of which short-term deposits – the most – by 6 percent points. At end-2009 short-term deposits had a major share in resident deposits (54.3%), while in non-resident deposits – demand deposits (54.6%) (compared to 50.9% and 62.3% at end-2008) (see Figure 18).

Figure 18
TERM STRUCTURE OF DEPOSITS
(as a percentage)

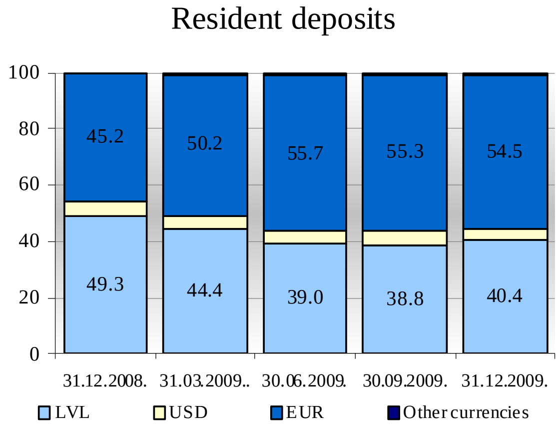


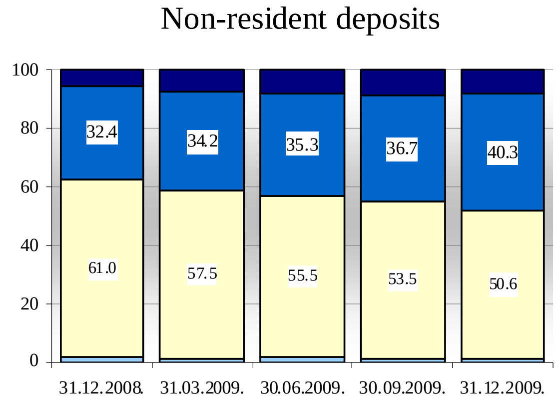
In the reporting year, the amount of deposits continued shrinking both in lats (by 552 million lats or 18.5%), and US dollars (by 508 million lats or 19.5%), while deposit stock in euro grew (by 762.5 million lats or 19.4%), therefore the structure of deposit currencies changed as well. By the end of the year the share of deposits in euro amounted to 54.5% of resident deposits, but deposits in lats made up 40.4% (compared to 45.2% and 49.3%, respectively, at end-2008), while the amount of US dollars (50.6%) still was the key currency of non-resident deposits and deposits in euro – 40.3% (compared 61% and 32.4% at end-2008) (see Figure 19).

Figure 19

DEPOSITS BROKEN BY CURRENCY

(as a percentage)





PERFORMANCE INDICATORS

In 2009, the banking sector overall ended the year with a 773.4 million lats loss (after tax), though nine banks (with market share of 16.2% in total banking assets) operated with profit earning the total of 19.6 million lats. Banks suffered significant losses mainly because of the loan loss provisioning. Operational profit of the banking sector (profit before provisioning and taxes) totalled 322 million lats in 2009, or by 21% down from 2008.

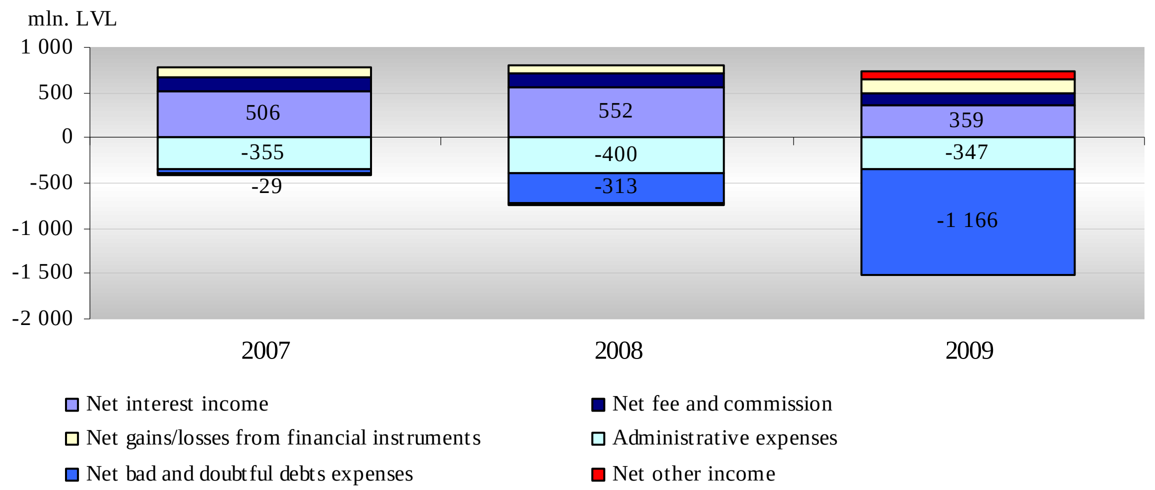
Income and expense structure

Negative lending growth rate and worsening of loan quality in the reporting year had the most adverse impact on the banking income and expense structure. In 2009, banks' net interest income notably contracted – following a decrease in the banking loan portfolio, also interest income from loans to non-MFI (by 28.4%), whereas with a decrease in banking total liabilities to MFI (by 20.2%) and interbank interest rates, also interest expenses on those attracted funds considerably fell (by 44.5%). In the reporting year, loan loss provisions notably increased having grown almost fourfold and totalling 1,166 million lats had the major impact on banking profit (see Figure 20).

In times of economic turmoil in 2009 when the activity of customers also was on the decline, the banking net fee and commission income fell by 20.6% y-o-y. Particular attention was paid on reduction of administrative expenses by cutting both the salaries and the number of bank employees were in the focus of banks in the reporting year, thus total administrative expenses of banking sector shrank by 13.4%. In the reporting year, banks succeeded in increasing banking income y-o-y from trading in foreign currencies and securities (by 18%), as well as revaluation of financial instruments (by 50.8%). In 2009, expenses on loan impairment provisions and liabilities (54%) were key expense item for the banks, while interest income from loans to non-MFI was still major income source of banks (51.1%) (compared to 19% and 61.3% at end-2008).

Figure 20

INCOME AND EXPENSE STRUCTURE



BANK EXPOSURES

Capital requirements for credit risk, market risk and operational risk

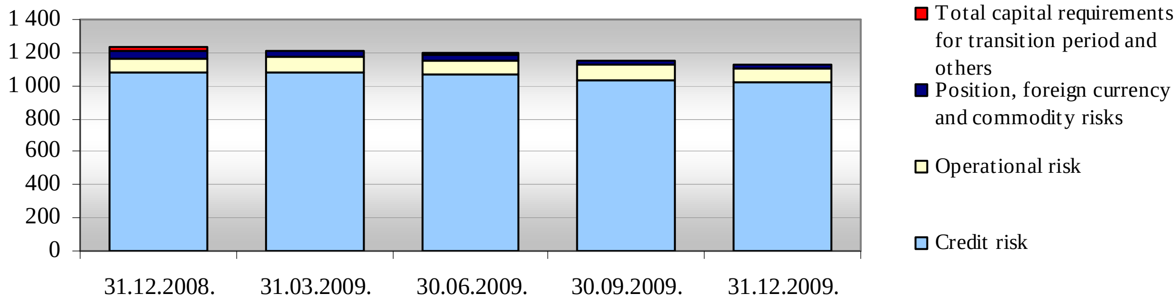
In 2009, the total amount of banking capital requirements[7] decreased by 81.6 million lats or 6.8%, i.e. following a decrease in loan portfolio, capital requirements for credit risk shrank the most – by 63.5 million lats or 5.9%. By end-December total amount of banking capital requirements made up 1,126.9 million lats, of which the greater share or 90.2% were capital requirements for the credit risk inherent in the banking book, 8.1% – capital requirement for operational risk and 1.7% – capital requirements for position, foreign currency and commodity risks (see Figure 21).

[7] The capital adequacy requirement reflects the bank's capital required for hedging against credit risk, market risks and operational risk.

Figure 21

BREAKDOWN OF CAPITAL ADEQUACY REQUIREMENTS

(million lats)

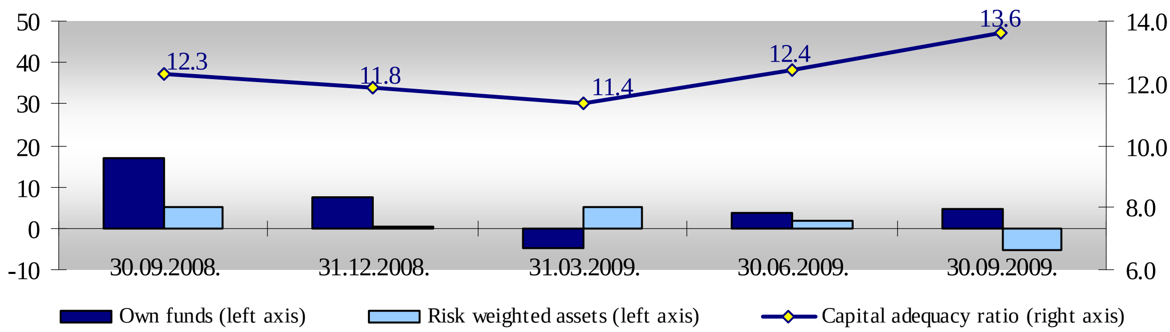


Following the ongoing deterioration in the banking asset quality and considering the necessity for notable additional provisioning for loan impairment, the banks attempted to strengthen their capital base in the reporting year – 13 Latvian banks increased their capital by about one billion lats in total, of which share capital by 728 million lats, subordinated capital by 222 million lats and reserves capital by 48 million lats. Upon an increase in the banking own equity by 14.7%, and a decrease in the amount of bank risk-weighted assets by 6.8% in the reporting year, capital adequacy ratio of the banking sector grew and at end-December totalled 14.6% (compared to 11.8% at end-2008) (see Figure 22.).

Figure 22

ANNUAL GROWTH RATE OF RISK-WEIGHTED ASSETS AND SHARE CAPITAL AND CAPITAL ADEQUACY RATIO

(as a percentage)



At end-2009 capital adequacy ratio for one bank varied from 9% to 10%, while for other banks was above 10% (see Table 2).

Table 2

BANK GROUPS BROKEN DOWN BY CAPITAL ADEQUACY RATIO

Capital adequacy ratio (%)	31.12.2008		31.12.2009	
	Number of banks	Banking market share (% of total banking assets)	Number of banks	Banking market share (% of total banking assets)
below 10	3	25.9	1	4.0
10.1–12	6	30.6	5	28.4
12.1–15	5	32.8	4	9.6
15.1–20	5	9.1	7	55.9
above 20.1	2	1.6	4	2.1

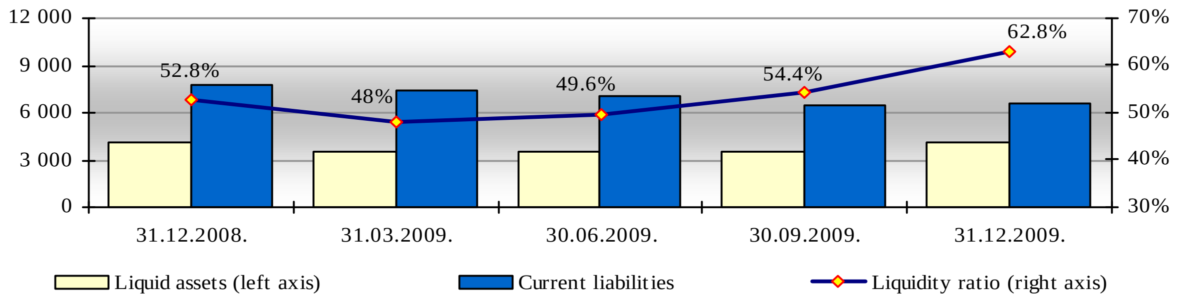
Liquidity risk

In 2009, the amount of liquid assets[8] in the banking sector rose by 1.4%, whereas following a continuous decrease in both the amount of deposits and liabilities to credit institutions, also the amount of current liabilities[9] fell by 14.8% and the liquidity ratio of the banking sector improved making up 62.8% at end-December (compared to 53% at end-2008) (credit institutions are obliged to maintain adequate liquid assets in sufficient amounts, but not less than 30% of total current liabilities) (see Figure 23).

Figure 23

LIQUID ASSETS, CURRENT LIABILITIES AND LIQUIDITY RATIO OF BANKS

(thousand lats; as a percentage)



At the end of reporting year, liquidity ratio for one bank varied between 38% and 40%, whereas for other banks – exceeded 40% (see Table 3).

[8] Liquid assets = vault cash + claims on central banks and other credit institutions + fixed-income debt securities of central governments.

[9] Current liabilities – claim liabilities and liabilities with a residual maturity of not more than 30 days.

Table 3

BANK GROUPS BROKEN DOWN BY THEIR LIQUIDITY RATIO

Liquidity ratio (%)	31.12.2008		31.12.2009	
	Number of banks	Banking market share (% of total banking assets)	Number of banks	Banking market share (% of total banking assets)
below 40	2	10.0	1	0.6
40.1–50	8	34.6	2	24.3
50.1–70	6	51.9	9	37.6
above 70.1	5	3.5	9	37.5

CONSOLIDATION GROUPS

Banking and financial holding company consolidated groups

At end-2009, 15 Latvia-registered banks running the groups subject to consolidated supervision, and one bank responsible for a financial holding group overall had 117 subsidiaries. A majority of banking subsidiaries were auxiliary undertakings (AUU) and other financial institutions (OFI), including institutions set up for managing alienated real estate until they are realized on the market (see Table 4).

Table 4

TYPES OF ACTIVITY OF SUBSIDIARIES INCLUDED IN BANKING CONSOLIDATION GROUPS

Type of subsidiary	31.12.2008		31.12.2009	
	total	incl. foreign	total	incl. foreign
Leasing companies (LEC)	25	13	26	13
Investment brokerage firms (IF)	8	5	9	5
Investment management companies (IMC)	12	-	13	-
Banks (BNK)	4	4	3	3
Pension funds (PFU)	5	-	5	-
Auxiliary undertakings (AUU)	17	4	41	5
Other financial institutions (OFI)	18	8	20	9
Total	**89**	**34**	**117**	**35**

In the reporting period, investments by the Latvian banking groups were mostly made in subsidiaries registered in Latvia (82), Russia (7), Ukraine (5) and Cyprus (6), as well as in Estonia (5), Lithuania (4), Belarus (3), Hungary (1) and in four more subsidiaries registered in non-European Union countries (see Table 5).

Table 5

SUBSIDIARIES INCLUDED IN BANKING CONSOLIDATION GROUPS

Banks and their subsidiaries	Type of company	Country
AS "Aizkraukles banka"		
AS "AB.LV Asset Management"	IMC	Latvia
AB.LV Capital Markets	IF	Latvia
SIA "Elizabetes 21a"	AUU	Latvia
KS AB.LV Transform Partnership	AUU	Latvia
AS "AB KONSULTĀCIJA"	AUU	Latvia
SIA "AB.LV Transform Investments"	AUU	Latvia
AB LV TRANSFORM 1	AUU	Latvia
AB LV TRANSFORM 2	AUU	Latvia
AB LV TRANSFORM 3	AUU	Latvia
AB LV TRANSFORM 4	AUU	Latvia
AB LV TRANSFORM 6	AUU	Latvia
AB LV TRANSFORM 7	AUU	Latvia
AB LV TRANSFORM 8	AUU	Latvia
AB LV TRANSFORM 9	AUU	Latvia
AB LV TRANSFORM 10	AUU	Latvia
AB LV TRANSFORM 11	AUU	Latvia
SIA "New Hanza City"	AUU	Latvia
SIA HAAS INVEST	AUU	Latvia
AS "GE Money Bank"		
IMC "GE Money Asset Management"	IMC	Latvia
AS "GE Money atklātais pensiju fonds"	PFO	Latvia
AS DnB NORD Banka		
SIA "DnB NORD Līzings"	LEC	Latvia
IMJS "DnB NORD Fondi"	IMC	Latvia
SIA "Skanstes 12"	OFI	Latvia
SIA "Salvus"	OFI	Latvia
SIA "Salvus2"	OFI	Latvia
SIA "Salvus 3"	OFI	Latvia
"Swedbank" AS		
SIA "Swedbank Līzings"	LEC	Latvia
"Swedbank Atklātais Pensiju Fonds" AS	PFU	Latvia
SIA "Swedbank Autoparku vadība"	LEC	Latvia
SIA "Hansa Apdrošināšanas Brokeris"	OFI	Latvia
SIA "Swedbank Īpašumi"	AUU	Latvia
AS "Latvijas Biznesa banka"		
Eesti Krediidipank AS	BNK	Estonia

Krediidipanga Liisingu AS	LEC	Estonia
Martinoza AS	AUU	Estonia
Valsts AS "Latvijas Hipotēku un zemes banka"		
SIA "Hipolīzings"	LEC	Latvia
SIA "Hipotēku bankas nekustamā īpašuma aģentūra"	AUU	Latvia
KS "Mazo un vidējo komersantu atbalsta fonds"	OFI	Latvja
SIA "Riska investīciju sabiedrība"	OFI	Latvia
AS "Hipo Fondi"	IMC	Latvia
AS "Latvijas Krājbanka"		
"Pirmais atklātais pensiju fonds"	PFU	Latvia
SIA "Baltic Property Projects"	AUU	Latvia
SIA "LKB Līzings"	LEC	Latvia
SIA "Krājinvestīcijas"	AUU	Latvia
IMC "LKB Asset Management"	IMC	Latvia
IMC "LKB Krājfondi"	IMC	Latvia
SIA "LKB drošība"	AUU	Latvia
AS IF "Renesource Capital"	IF	Latvia
AS "LKB Collect"	AUU	Latvia
AS "SMP Bank"		
AS "SMP Finance"	OFI	Latvia
AS "NORVIK BANKA"		
AS "NORVIK Ieguldījumu pārvaldes sabiedrība"	IMC	Latvia
NORVIK UNIVERSAL CREDIT ORGANISATION CJSC	OFI	Armenia
SIA "NORVIK LĪZINGS"	LEC	Latvia
IPS NORVIK ALTERNATIVE INVESTMENTS AS	IMC	Latvia
AS "Parex banka"		
IMJS "Parex Asset Management"	IMC	Latvia
"Regalite Holdings Limited"	AUU	Cyprus
JSC "Parex Bankas"	BNK	Lithuania
SIA "Parex Express Kredīts"	OFI	Latvia
AS "Parekss atklātais pensiju fonds"	PFU	Latvia
OU "Parex Leasing &Factoring"	LEC	Estonia
"Parex Asset Management"	IF	Russia
OOO "Aktīvu pārvaldīšanas kompānija un pensiju fondu administrators –"Parex Asset Management Ukraina"	IF	Ukraine
SIA "E&P Baltic Properties"	IMC	Latvia
UAB "Parex faktoringas ir Lizingas"	LEC	Lithuania
UAB "Parex investiciju valdymas"	IF	Lithuania
AP Anlage & Privatbank AG	BNK	Switzerland
OOO "Pareks Lizing and Faktoring"	LEC	Azerbaijan
OOO "Ekspress lizing"	LEC	Russia

OOO "Laska Lizing"	LEC	Ukraine
OOO "Parex lizing"	LEC	Russia
OOO "Parex lizing"	LEC	Belarus
OOO "Extroleasing"	LEC	Russia
Calenia Investments Limited	AUU	Cyprus
SIA "Parex Līzings un faktorings"	LEC	Latvia
SIA "Rīgas Pirmā Garāža"	AUU	Latvia
OOO "Extrocredit"	OFI	Russia
SIA "Parex Private Banking"	AUU	Latvia
LLC "Parex Leasing and Factoring"	LEC	Georgia
SIA "RPG interjers"	AUU	Latvia
OOO "Pareks Investments Ukraina"	IF	Ukraine
Parex Ukrainian Equity Fund	IF	Ukraine
SIA "PR Speciālie Projekti"	AUU	Latvia
SIA "NIF"	AUU	Latvia
SIA "NIF Dzīvojamie īpašumi"	AUU	Latvia
SIA "NIF Komercīpašumi"	AUU	Latvia
SIA "NIF Zemes īpašumi"	AUU	Latvia
UAB "Nekilnojamojo turto valdymo fondas"	AUU	Lithuania
OU "Restruktureeritud Kiinisvarafond"	AUU	Estonia
AS "PrivatBank"		
SIA "PrivatLīzings"	LEC	Latvia
SIA "PrivatConsulting"	AUU	Latvia
SIA "Amber Real"	AUU	Latvia
AS "Rietumu Banka"		
AS "RB securities IBS"	IF	Latvia
"RB Securities Limited"	OFI	Cyprus
AAS "RB Securities"	OFI	Russia
AS "RB Asset Management" IPS	AUU	Latvia
SIA "RB Investments"	OFI	Latvia
SIA "Vesttransinvest"	LEC	Belarus
ASIA "Vestlizing"	LEC	Belarus
SIA "Oshadna Kompanija"	OFI	Ukraine
"V7 Holding Limited"	OFI	Cyprus
"B54 Holdings Limited"	OFI	Cyprus
SIA "Frb Elektro"	OFI	Latvia
SIA "Vestlizing-M"	LEC	Russia
AS "SEB Latvijas Unibanka"		
AS atklātais pensiju fonds "SEB pensiju fonds"	PFU	Latvia
Investīciju sabiedrība "SEB Wealth Management"	IMC	Latvia
SIA "SEB līzings"	LEC	Latvia
SIA "SEB Enskilda"	IF	Latvia

SIA "Latectus"	AUU	Latvia
AS "Trasta komercbanka" SIA "TKB Līzings" SIA "TKB nekustamie īpašumi" *Ferrous Kereskedelmi Limited* *Heckbert C7 Holdings Limited*	 LEC AUU OFI OFI	 Latvia Latvia Hungary Cyprus
AS "VEF banka" SIA "Veiksmes līzings"	 LEC	 Latvia
AS "Akciju komercbanka "Baltikums" (finanšu pārvaldītājsabiedrību konsolidācijas grupa) SIA "Konsalting Invest" SIA "Baltikums Līzings" IPS "Baltikums Asset Management" SIA "CityCap Service" SIA "ZapDvinaDevelopment"	 OFI LEC IMC AUU AUU	 Latvia Latvia Latvia Latvia Latvia

The share of assets of the bank subsidiaries in the parent bank assets contracted in 2009 and at end-December made up 15.5% (compared to 17.7% on 31 December 2008). The major share in total assets of subsidiaries constituted leasing companies, 53.2%, banks – 23.3% and investment management companies, 10.4% (compared to 56.1%, 24.8% and 9.1% on 31 December 2008).

At end-2009, the capital adequacy ratio calculated basing on the consolidated financial statements of banks and financial holding groups was 13.7%.

LOAN PORTFOLIO OF BANK SUBSIDIARIES

Economic downturn affected also the amount of loans issued by the subsidiaries of banks (leasing companies, banks and other financial institutions, basic business activity of which is crediting) contracted notably in 2009, i.e. by 699 million lats, or 30.8%, and at end of December totalled 1.6 billion lats, or 10.2% of bank loan portfolio (compared to 13.7% on 31 December 2008).

Approximately a half of total loan portfolio of bank subsidiaries was issued for Latvian economic lending, of which the greater proportion was made up of loans issued to such sectors as transport and storage (10%), trade (9.2%), as well as manufacturing industry (6.8%) (compared to 10.6%, 8.4% and 7.4% on 31 December 2008). Whereas 14% of loan portfolio of bank subsidiaries were granted to resident households by end of year (compared to 12% on 31 December 2008). As a number of subsidiaries provided their services in foreign countries, 33.5% of total credit portfolio was issued to non-residents (compared to 31.5% on 31 December 2008).

The quality of banking subsidiaries' loan portfolio was also affected adversely by the economic situation which notably deteriorated in 2009 and by the end of the year 65.4% of total loans issued by those subsidiaries were without payment delays while the share of loans with payments overdue more than 90 days rose by 16.1% (compared to 74% and 6.3% on 31 December 2008).