



## Baltikums Bank AS 2016 Capital Adequacy Assessment Process Report

## 1. General description of the Bank, core lines of business, conclusion regarding the Bank's strategic planning

- 1.1. Baltikums Bank AS (hereinafter referred to as the Bank) is a credit institution registered in the Republic of Latvia, operating to provide client service in a dynamic, modern, exclusive paradigm built around client-oriented financial services. The Bank develops a state of the art financial platform for business and asset management worldwide. The Bank's mission for:
  - 1.1.1. our clients and partners:
    - 1.1.1.1. always adapting to client needs and keeping their interests at the core of our business;
    - 1.1.1.2. quick and effective solutions for global commerce;
    - 1.1.1.3. individual approach to each client for sustainable relationships
  - 1.1.2. our bank:
    - 1.1.2.1. state of the art financial technologies with a view to improve day-to-day usability and accessibility of financial services
    - 1.1.2.2. openness to innovations and generation of creative ideas
    - 1.1.2.3. exceptional standards of security and reliability
  - 1.1.3. our people:
    - 1.1.3.1. a great place to work for talented people
    - 1.1.3.2. engaging work that makes talent feel inspired
    - 1.1.3.3. a corporate culture built on trust, freedom of communication, and encouragement for initiative
- 1.2. Adequate capital maintenance and risk management strategy at the Bank:
  - 1.2.1. A major aspect considered by the Bank is careful risk management. The strategy of the Bank entails the acceptance of certain financial and non-financial risks.
  - 1.2.2. A priority of Bank management is the maintenance and expansion of the assets of its clients and shareholders, and maintenance of a good reputation. The Bank focuses on profit through reasonable commercial risk.
  - 1.2.3. The general risk management guideline is to assume only those risks which the Bank understands clearly and is able to manage effectively. The Bank assumes moderate interest rate, currency, country and market risks. Aware of the potential variations in its resource base, the Bank maintains a sufficiently high amount in liquid assets to keep liquidity risk at moderate levels. In terms of credit risk, the Bank intentionally targets investments for which the Bank understands the risks involved, thereby enabling various degrees of concentration across certain types of investment: financing priorities, positions in Eastern European issuers' fixed-income securities. The Bank pays great attention to reputational and operational risk and considers only minimal levels of these risks to be acceptable.
  - 1.2.4. In its operations, the Bank implements a broad risk control mechanism, leveraging modern IT solutions wherever feasible.
  - 1.2.5. In planning its activities and managing risks, the Bank considers, analyses, evaluates and documents potential development scenarios for the Bank depending on the development scenarios of various external conditions, considering further the development of various macroeconomic indicator scenarios in the countries in which the Bank conducts or plans to conduct its operations – which may also affect the Bank's operations – as well as potential industry development trends, likely amendments to laws, regulations and standards, the activities of competition, and other factors that have a substantial impact on the achievement of the Bank's overarching goals.
  - 1.2.6. Considering that the Bank has an additional/individually defined capital requirement due to its operations in large part being related to servicing non-resident clients, and the fact the additional capital requirement is substantial compared to the 8% capital requirement specified in the EU Capital Requirements Regulation (CRR, EU Regulation 575/2013), the Bank maintains a level of capital adequacy that can ensure adherence to the individual capital requirement in the event of manifestation of scenarios in which the Bank might sustain considerable losses.
  - 1.2.7. The Bank's capital adequacy targets are specified in the Bank's Strategy. To maintain capital adequacy at the level specified in the Strategy, the Bank ensures capital adequacy planning with a 4-year horizon, preparing its financial budgets and planning its financial indicators. The Bank specifies quantitative indicator targets for each individual risk.
  - 1.2.8. The Bank develops a management system for each specific risk and for the Bank's overall capital adequacy management, as described in relevant policies and procedures (*Capital Adequacy Management Policy, Credit Risk Management Policy, Liquidity Management Policy, Non-Financial Risk Management Policy, AML/CFT Policy etc.*). Among other things, the aforementioned management system specifies actions to maintain acceptable risk levels; a plan to achieve desired capital levels; sources of financing to supplement capital; expected costs of attracting further capital; a plan for ensuring adherence to capital adequacy regulations; and an emergency capital adequacy maintenance plan.
  - 1.2.9. The Bank has structural divisions in place, independent from business, which are tasked with implementing

risk and compliance functions. The bank has established an Internal Audit Service in order to provide impartial assessment.

- 1.2.10. An important task for the Bank is ongoing development coupled with enhancements to its internal control system (including sound risk management).
- 1.3. Leverage ratio and excessive leverage risk:
- 1.3.1. In accordance with CRR requirements, aiming to improve the stability of the financial market, a new supervisory instrument will be introduced by 2018 – the Leverage ratio; banks will be tasked with monitoring their leverage ratios and changes thereto as part of their internal capital adequacy assessment processes. In accordance with CRR and CRD IV requirements, supervisory bodies are to develop effective limits on the leverage ratio and specify them on account of the business profile and risk profile of each institution.
- 1.3.2. In accordance with the CRR, Leverage is the ratio of: a bank's assets, liabilities and potential liabilities off the balance sheet to be paid, executed or secured, including liabilities for financing received, guarantees issued, derivative instruments, or agreements on the sale or buyback of assets – not including liabilities that may only be realised in the event of liquidation of the institution – to the institution's equity.
- 1.3.3. Excessive leverage risk is the risk arising due to an institution's vulnerability caused by actual or potential leveraging in its financing structure, and which may bring about unexpected corrective measures regarding the business plan, including any sale of assets due to financial difficulties that may lead to losses or adjustments to the value of residual assets. The leverage ratio is calculated as the value of a bank's tier 1 capital divided by the value of the bank's total risk-bearing transactions, and expressed as a percentage. The value of total risk assets represents the sum of all risk-bearing transactions under assets and items off the balance sheet not deducted in the course of specifying tier 1 capital.
- 1.3.4. The Bank reports information on the calculated leverage ratio as part of its quarterly reports to the supervisory body; in 2016, the ratio equalled:

Periods	Leverage ratio (%)
2016 Q1	7.67%
2016 Q2	7.00%
2016 Q3	7.50%
2016 Q4	8.65%

Leverage ratio calculation summary as at 31.12.2016.:

Balance sheet risk-bearing transactions (except derivatives and SFTs)		
1	Balance sheet items (excluding derivatives, SFTs and fiduciary assets, but including collateral)	650 247 885
2	(Amounts of assets deducted from the calculation of tier 1 capital)	(1 748 440)
3	<b>Total risk-bearing transactions on the balance sheet (except derivatives, SFTs and fiduciary assets) (sum of items 1 and 2)</b>	648 499 445
Derivatives transactions		
4	Replacement value for all derivatives transactions (i.e. without deducting the relevant variable monetary safety reserve)	89 576
5	Amounts of increase in potential future risk of all derivatives transactions (market value method)	164 627
<...>		
11	<b>Total risk-bearing derivatives transactions (sum of items 4 through 10)</b>	254 203
Other risk-bearing transactions off the balance sheet		
17	Gross tentative amount of risk-bearing transactions off the balance sheet	55 459 163
18	(Adjustment to the calculation of credit-equivalent amounts)	(41 570 448)
19	<b>Other risk-bearing transactions off the balance sheet (sum of items 17 and 18)</b>	13 888 715
Value of capital and total risk-bearing transactions		
20	<b>Tier 1 capital</b>	57 303 985
21	<b>Total risk-bearing transactions for Leverage purposes (sum of items 3, 11, 16, 19, EU-19.a and EU-19.b)</b>	662 642 363
Leverage ratio		
22	<b>Leverage ratio</b>	8.65%

## 2. Capital adequacy assessment process

- 2.1. The purpose of the capital adequacy assessment procedure is to evaluate all risks borne by the Bank and maintain adequate coverage of these risks with available capital.
- 2.2. The procedure of internal evaluation of the Bank's capital adequacy is specified in the Bank's Capital Adequacy Management Policy.
- 2.3. Internal evaluation of capital adequacy is performed on a quarterly basis, within one month following the end of a calendar quarter.
- 2.4. The Bank's capital is evaluated as either "adequate" or "inadequate" by the Bank's Investment Committee (IC). All calculations are performed by the Financial Analysis and Financial Risk Management Department, in accordance with the procedure specified in the Bank's Capital Adequacy Management Policy and annexes thereto, using assumptions specified by the IC where applicable.
- 2.5. On the basis of FCMC Regulations on the Internal Capital and Liquidity Adequacy Assessment Process, the Bank defines:
  - 2.5.1. the total capital requirement (TSCR);
  - 2.5.2. the total capital reserve requirement;
  - 2.5.3. the capital guidance (recommended capital reserve);
  - 2.5.4. the overall capital requirement (OCR) – sum of TSCR, capital reserve requirement, and capital guidance;
  - 2.5.5. the amount of capital at the Bank's disposal.
- 2.6. The Bank employs the simplified methods specified in the FCMC Regulations on the Internal Capital and Liquidity Adequacy Assessment Process for evaluating credit risk, concentration risk, debt securities price risk, currency risk and operational risk capital requirements. The Bank employs in-house approaches and methodologies to determine capital requirements for liquidity risk, interest rate risk in the non-trading portfolio, miscellaneous risks (including money laundering/terrorist financing risk, reputational risk, strategy and business risk, and other risks):
  - 2.6.1. Capital requirements for credit risk (applies to the Bank's claims on credit institutions and other counterparties, loans to clients, investments in debt securities, and investments in other assets) include all capital requirements which, in accordance with EU Regulation 575/2013, apply to credit risk, as well as concentration risk (additional credit risk related to loans to clients and investments in bonds) calculated using the FCMC Regulations on the Internal Capital and Liquidity Adequacy Assessment Process. In addition to capital requirements determined using the aforementioned simplified methods, the Bank also conducts stress testing of credit risk related to client loans (including loans taken over), stress testing of credit risk related to investments in debt securities, and assessment of credit risk related to claims on other credit institutions and counterparties, and if potential losses determined using stress testing or assessment exceed capital requirements determined using simplified methods, the difference between potential losses determined using stress testing or assessment and capital requirements determined using simplified methods is included in the capital reserve amount:
    - 2.6.1.1. Stress testing of credit risk related to loans issued to clients (excluding securities-backed loans) is performed in accordance with the Methodology for Stress Testing Loan Credit Risk. For each loan, the probability of default in a "bad" year is assumed based on an evaluation of the loan's credit capacity, or rating (according to the negative scenario) and the Bank's assumed losses in the event of the borrower's default. Potential losses for the Bank are then determined using the Monte Carlo method. The total of potential losses is combined with the potential of losses due to loan portfolio concentration across various dimensions, and residual risk, in order to come up with total potential losses for the Bank;
    - 2.6.1.2. Stress testing of credit risk related to the Bank's investments in debt securities and loans against debt securities is performed using the Securities Credit Risk Stress Testing Methodology;
    - 2.6.1.3. The calculation of potential losses is based on the assumption that the probability of default in the obligations of issuers is characterised by, and may be predicted based on, historical data about default (non-performance) by issuers maintained by the Moody's ratings agency, available as a list of defaulting issuers grouped by credit capacity rating. Potential (1 year) losses are calculated with the assumption that the amount of investments in securities and loans against securities, as well as the distribution of this volume among issuers with specific credit capacity ratings will remain unchanged during the subsequent 12-month period (i.e. other securities with the same rating as redeemed securities will be purchased). Thus, potential losses are calculated regardless of the remaining maturity terms of such securities, factoring in only the credit capacity of the issuers;
    - 2.6.1.4. during calculation of potential losses, the likelihood of (partial) recovery of investments in the event of default by an issuer (also known as the Recovery Rate) is considered;
    - 2.6.1.5. to calculate potential losses, 1000 tests/simulations are performed, and in each of the tests each issuer may potentially default or not default based on the relevant default probability. Losses from investments in the securities of each issuer in the event of default are calculated by multiplying the total of the Bank's investments and loans by  $(1 \text{ minus recovery rate})$ ; the total of losses from all defaults by all issuers thus constitutes the Bank's total potential losses for the relevant test/simulation. Potential losses of the Bank are calculated as total losses in the 40th worst (by total

- losses) test/simulation out of the 1000;
- 2.6.1.6. default probabilities for the subsequent 12-month period in the negative stress testing scenario use the ratio of total defaulting issuers (by rating) to the total number of issuers (by rating) observed in 2009, the year following a financial crisis when the ratio of issuers in default was one of the highest observed in 31 years (from 1983 to 2013);
- 2.6.1.7. assessment of credit risk related to claims on other credit institutions and counterparties is performed by the Bank's IC, considering concentration of the Bank's claims among various counterparties and countries;
- 2.6.2. The capital requirements for debt securities price risk and currency risk are consistent with capital requirements specified in EU Regulation 575/2013. In addition to the capital requirements specified using the aforementioned simplified methods, the Bank also performs stress testing of these risks; if potential losses determined using stress testing or assessment exceed capital requirements determined using simplified methods, the difference between potential losses determined using stress testing or assessment and capital requirements determined using simplified methods is included in the capital reserve amount:
- 2.6.2.1. stress testing of market risk for bonds is performed in accordance with the Debt Securities Market Risk Stress Testing Methodology. Stress testing determines potential losses that the Bank might sustain in the event of a major market crisis and ensuing decrease in the value of securities in its trading and available-for-sale portfolio (1 month scenario), as well as if the Bank should be forced to liquidate the entirety of its securities portfolios (including the investment portfolio) 1 year following the date of the stress testing with the assumption that the prices of such securities would be at historically low levels at that point (1 year scenario);
- 2.6.2.2. to calculate potential losses for the Bank due to potential decrease in debt securities prices, maximum expected bond revenue levels are specified (depending on credit capacity ratings) given a stress situation. It is assumed that the likely level of bond income under market stress would be characterised by the highest income on 63 Russian and CIS country issuers' bonds observed during the period of time from October 2014 till February 2015:

Rating	Number of issuers	Max median yield Oct 14-Feb 15, %	Stress scenario yield, %
BBB	8	7.4%	7.4%
BB	36	11.6%	11.6%
B+ to B	14	16.1%	16.1%
B- to C	5	13.9%	20.0%

for highly rated debt securities ranging from AAA to A-, custom stress scenario yield of between 0.5% and 3% is assumed on a case by case basis;

- 2.6.2.3. the results of internal capital adequacy assessment include "1 year" scenario results. For bonds with a term to maturity that exceeds 1 year as at the date of stress testing, the stress scenario price is calculated using the Excel PRICE formula at the date 1 year following the stress testing date, given stress scenario income for the relevant credit rating, and for bonds with a term to maturity of no more than 1 year following the stress testing date, the Bank's potential losses are calculated as the difference between the value of a bond at market price and at price = 100; Potential losses are calculated as the difference between the current balance sheet value of a security and its stress testing value (divided by 100) and multiplied by the balance sheet value of the relevant security. The "1 year" scenario includes the Bank's expected income from securities coupons;
- 2.6.2.4. currency risk stress testing calculates potential losses to the Bank from potential changes in exchange rates (within 1 day). The period of holding a position for 1 day has been selected because the periodicity of holding positions is actually short (the Bank does not maintain a position in any currency long-term), and the Bank is capable of closing any position within a short span of time. To calculate potential losses, the (absolute) value on the position stress testing date (for positions worth > EUR 70 thous.) is multiplied by the largest change in the value of the relevant currency (against EUR) within 1 day during the period since the beginning of 2008;
- 2.6.3. interest rate risk in the Bank's non-trading portfolio is evaluated in accordance with the procedure specified in the Interest Rate Risk Management Policy. If the IC has identified/assessed interest rate risk as significant, the Financial Analysis and Financial Risk Management Department conducts stress testing of interest rate risk quarterly within the framework of its internal assessment of capital adequacy, calculating the potential impact of changes in base interest rates (in the currencies significant for the Bank) on the Bank's net interest income (non-trading portfolio) and, if stress testing calculations show that the Bank's net interest income

- as a result of changes in interest rates might be negative, the potential losses are considered the capital requirement for this risk;
- 2.6.4. The liquidity risk capital requirement is determined based on liquidity risk stress testing results. If stress testing indicates that liquidity risk stress scenarios could produce a deficit of liquid assets for the Bank, potentially requiring attraction of additional (external) financing for the Bank to maintain its operations and meet regulatory liquidity criteria, then expenses that might be related to attracting such emergency assets are evaluated, and these expenses are considered the liquidity risk capital requirement. The procedure of stress testing liquidity risk is described in clause 2.6.5 of this report;
- 2.6.5. The operational risk capital requirement is defined as the larger of two values: the operational risk capital requirement determined using the basic indicator approach specified in EU Regulation 575/2013 575/2013, and the value of potential operational risk losses determined/estimated by the Bank's Operational Risk Management Department (over a 1-year period);
- 2.6.6. Other risks (including strategy, business model, ML/TF and reputational risks):
- 2.6.6.1. As specified in clause 2.5 of this report, the Bank assumes the risks of its strategy, business model, ML/TF and reputational risks, and believes that the worst-case scenario that might occur if the aforementioned risks manifest themselves, is (1) major decrease in client deposits and (2) major decrease in income from fees. The potential decrease in client deposits is included in liquidity risk stress testing, while the risk of decreased income from fees is calculated in the manner outlined below;
- 2.6.6.2. the fee income risk is calculated as the difference between the total of the Bank's administrative expenses (annualised based on the preceding quarter) and 50% of the Bank's net fee income and currency trading income during the preceding 12 months: if the amount of administrative expenses of the Bank exceeds 50% of its net fee and foreign exchange income total, then the relevant positive difference is considered the Bank's fee income risk in accordance with clause 2.6.6.3 below; otherwise, fee income risk is assumed to be zero;
- 2.6.6.3. In accordance with FCMC policy, because the Bank's activity involves servicing of international (non-resident) clients, the Bank must maintain a significantly higher minimum capital adequacy indicator, which in the context of internal capital adequacy assessment is treated as equivalent to assuming substantially increased strategy/business model, ML/TF and reputational risks (hereinafter referred to as the "non-resident business capital requirement"). Therefore, the degree of risk of reduced fee income as calculated in accordance with clause 2.6.6.2 above (provided that it exceeds 0) is compared to the non-resident business capital requirement calculated as follows: (Individual capital adequacy indicator specified for the Bank, i.e. 10.5%) x the Bank's risk-weighted assets, and, if the non-resident business capital requirement exceeds the risk of reduced fee income, the risk of reduced fee income is assumed sufficiently covered by defining the individual capital adequacy indicator of the Bank; consequently, there is no need for additional capital to cover this risk.
- 2.6.7. The capital requirement for covering other risks is calculated as 5% of the total of minimal regulatory capital requirements.
- 2.7. TSCR and OCR:
- 2.7.1. The Bank calculates the total capital requirement for covering risks (TSCR) as the total of capital for covering pillar 1 risk and pillar 2 risk;
- 2.7.2. The Bank defines the capital guidance as the total of (1) additional capital necessary for covering risks (to ensure that the Bank's capital is sufficient for the occurrence of unfavourable scenarios significant for the Bank, as well as to ensure the Bank's capital adequacy throughout the economic cycle) and (2) minimum capital necessary for the Bank in the aforementioned negative scenarios to maintain operations, i.e. observe the capital adequacy requirement;
- 2.7.3. To determine the capital guidance:
- stress testing or evaluation is performed with regard to risks for which the capital requirement is determined using simplified methods, and the amounts of potential losses obtained using stress testing/evaluation are compared to capital requirements specified using simplified methods. If the amount of potential losses obtained using stress testing/evaluation exceeds capital requirements specified using simplified methods, the exceedance is added to the total capital reserve;
  - if the minimum amount of capital that the Bank would require to maintain operation following the manifestation of aforementioned negative scenarios exceeds the additional capital requirement related to the individually specified capital adequacy ratio, the exceedance is added to the total capital reserve;
- 2.7.4. The minimum capital that might be necessary for the Bank to continue operation, i.e. maintain the capital adequacy indicator in significant negative scenarios, is calculated by multiplying the expected total value of risk-weighted assets following all significant losses from all significant risks (considering further the withdrawal of deposits due to the liquidity risk stress scenario) and measures to maintain capital adequacy, by the forecast increased individual minimum capital adequacy indicator specified for the Bank following the occurrence of the aforementioned;

- 2.7.5. The Bank calculates the amount of OCR as the total of the TSCR, the capital maintenance reserve, the countercyclical capital reserve specific to the institution, and the capital guidance.
- 2.8. Capital at the Bank's disposal:
  - 2.8.1. For the purpose of evaluating capital at the Bank's disposal, the Bank defines such capital as its net worth, calculated on the basis of EU Regulation 575/2013 by adding 50% of the unaudited, undistributed profit for the reporting year (and prior years), considering the dividend payment policy/plans and the fact that undistributed profits are fully available for coverage of sudden losses should such losses arise;
  - 2.8.2. The decision to include unaudited undistributed profit in capital at the Bank's disposal is made by the IC (each time that internal assessment of capital adequacy is performed), evaluating whether the undistributed profit would be available for coverage of potential losses.
- 2.9. Following assessment TSCR, OCR, and capital at the Bank's disposal, the capital excess/deficit is calculated in the interpretation of FCMC Regulations on the Internal Capital and Liquidity Adequacy Assessment Process as the difference between capital at the Bank's disposal and the total capital requirement.
- 2.10. Considering that the overall capital requirement includes potential losses (capital requirements) for all major risks in stress scenarios as well as the minimum capital for maintaining operations based on the increased minimum capital adequacy requirement applied to the Bank, the Bank assumes that its OCR may exceed the amount of capital available to the Bank – the Bank may face a shortage of capital in the interpretation of the FCMC "Normative regulations on establishing a capital and liquidity adequacy assessment process"; however, in evaluating its capital as "adequate" or "inadequate", the Bank also considers available measures to mitigate risk/increase capital, which the Bank could relatively easily and without significant additional expenses implement in order to increase its capital adequacy indicator. Such measures include:
  - 2.10.1. liquidating the Bank's securities portfolio;
  - 2.10.2. investing in 0%-risk assets;
  - 2.10.3. limiting lending operations, including refusal to extend reverse-repo loans.
- 2.11. If calculations show that, following potential losses in all significant risks, available measures specified in clause 2.10 would produce a higher than minimal individual capital adequacy indicator for the Bank, then the Bank's capital may be assessed as "adequate". If calculations show that, following potential losses on analysis significant risks and available measures specified in clause 2.10 would produce a lower than minimal individual capital adequacy indicator for the Bank, the Bank's Capital Adequacy Management Policy specifies appropriate measures to inform the Board and Council of the Bank and the FCMC, as well as actions to ensure that the calculated potential capital adequacy is no less than the specified individual minimum value.
- 2.12. In order to evaluate the adequacy of additional capital, the Bank's Capital Adequacy Management Policy also specifies capital/capital adequacy planning measures performed within the framework of planning the Bank's budget.

## 3. Overview of the results of the capital adequacy assessment process

3.1. Calculation of capital necessary to cover risks as at 31.12.2016.:

Capital necessary to cover risks			
	Item code	Credit institution's assessment of the capital requirement, including total capital reserve requirement under the Credit Institution Law	Additional information: capital requirement under EU regulation No. 575/2013, in accordance with paragraph 23
<b>Pillar I risks (1.1.+1.2.+1.3.+1.4.)</b>	<b>1.</b>	<b>29 467 392</b>	<b>29 467 392</b>
Credit risk	1.1.	24 821 405	24 821 405
Credit value adjustment (CVA) risk	1.2.		
Market risks (1.3.1.+1.3.2.+1.3.3.+1.3.4.), incl.:	1.3.	167 993	167 993
<i>foreign exchange risk</i>	1.3.1.	72 340	72 340
<i>settlement risk</i>	1.3.2.		
<i>goods risk</i>	1.3.3.		
<i>position risk</i>	1.3.4.	95 653	95 653
Operational risk	1.4.	4 477 994	4 477 994
<b>Pillar II risks (2.1.+2.2.+2.3.+2.4.+2.5.+2.6.)</b>	<b>2.</b>	<b>11 786 957</b>	
Interest rate risk in the non-trading portfolio	2.1.	-	
Concentration risk (2.2.1.+2.2.2.+2.2.3.+2.2.4.), incl.:	2.2.	3 232 940	
<i>individual concentration risk</i>	2.2.1.	1 646 541	
<i>industry concentration risk</i>	2.2.2.	1 501 749	
<i>currency mismatch concentration risk</i>	2.2.3.	84 650	
<i>collateral concentration risk</i>	2.2.4.	-	
ML/TF risk	2.3.	5 775 586	
Liquidity risk	2.4.	-	
Miscellaneous risk (2.5.1.+2.5.2.+2.5.3.), incl.:	2.5.	1 473 370	
<i>reputational risk</i>	2.5.1.	-	
<i>business model risk</i>	2.5.2.	-	
<i>other risks*</i>	2.5.3.	-	
Additional capital requirement for the individually specified capital adequacy ratio (round((if (1.+2.1.+2.2.+2.3.+2.4.+2.5.<7.*6./100; 7.*6./100-(1.+2.1.+2.2.+2.3.+2.4.+2.5.);0);0))	2.6.	1 305 061	
<b>Effects of diversification</b>	<b>3.</b>		
<b>Total capital reserve requirement (4.1.+4.2.+4.3.+4.4. or 4.1.+4.2.+max(4.3.; 4.4.)), incl.:</b>	<b>4.</b>	<b>9 392 731</b>	
<i>capital maintenance reserve</i>	4.1.	9 208 560	
<i>countercyclical capital reserve</i>	4.2.	184 171	
<i>other systemically significant institution capital reserve</i>	4.3.	-	
<i>systemic risk capital reserve</i>	4.4.	-	
<b>Capital guidance</b>	<b>5.</b>		

\* The credit institution provides a list of risks based on the classification of risks adopted by the credit institution.

### 3.2. Capital guidance calculation:

- 3.2.1. part of capital guidance necessary to ensure adequacy of the credit institution's capital for covering losses as a result of the manifestation of scenarios substantially unfavourable for the credit institution's operation (calculated using the results of testing substantial risks):

Risk	Risks determined upon assessment/stress testing			Capital requirement (simplified method)	Capital reserves for additional risk
	1 <sup>st</sup> year	2 <sup>nd</sup> year	total		
Credit risk of the Bank's demands on other credit institutions and counterparties	8 000	-	<b>8 000</b>	<b>5 836</b>	<b>2 164</b>
Credit risk and concentration risk of Bank loans to clients, excluding securities-backed loans	20 940	2 230	<b>17 253</b>	<b>11 700</b>	<b>5 553</b>
Interest income from loans to clients, excluding loans secured by bonds	-4 162	-1 755			
Credit risk of loans and investments in company capital taken over by the Bank	2 917	-	<b>2 917</b>	<b>614</b>	<b>2 303</b>
Credit risk of the Bank's investment in securities and securities-backed loans	1 000	-	<b>1 000</b>	<b>7 273</b>	<b>0</b>
Market risk of investment in debt securities	100	-	<b>100</b>	<b>96</b>	<b>4</b>
<b>TOTAL</b>					<b>10 024</b>

- 3.2.2. part of capital guidance necessary for maintaining minimum capital in order to continue the Bank's operations in the event of manifestation of negative scenarios – maintenance of the capital adequacy ratio. The amount of this part of capital guidance equals EUR 13.14 million. The calculation is based on the fact that the amount of risk-weighted assets will reach EUR 146 mio. within 1 year following the manifestation of unfavourable scenarios, while the forecast minimum individual capital adequacy ratio requirement will, considering the substantial decrease in non-resident deposits as a result of manifestation of liquidity risk stress test events, reach 8.6% (without a capital maintenance buffer and countercyclical capital buffer, for which capital reserves are calculated separately). In parallel, measures will be taken to improve capital adequacy, and the credit portfolio will be amortised. The measures include:

- Reducing/liquidating investments in bonds, including the discharge of obligations at (maturity) – except investments in longer-term bonds that may become illiquid – as well as to reduce/liquidate the portfolio of loans backed by securities (repo);
- Investing up to EUR 120 mio. in 0%-risk assets on a correspondent account with the Bank of Latvia and in 0%-risk sovereign bonds;

- 3.2.3. the minimum required capital adequacy indicator ratio in this case is set at 9.0% without additional buffers. The capital reserve value is obtained by multiplying forecast risk-weighted assets by the desired forecast value of the capital adequacy indicator;

- 3.2.4. the capital guidance is specified as EUR 0 mio.: as at 31.12.2016, the amount of capital necessary in order to cover overall losses calculated via stress scenarios equalled EUR 29.3 mio. The part of reserves necessary in order to maintain minimum capital as necessary for sustaining the Bank's operations following manifestation of negative scenarios (adhering to the capital adequacy requirement) equalled EUR 13.1 mio. The total amount was EUR 42.4 mio. The total of TSCR and overall capital reserve requirements adds up to EUR 50.7 mio. This means that, in accordance with Paragraph 68 of the Regulations, the Bank is not required to maintain additional capital reserves, and the amount of the capital guidance would be EUR 0 mio.

### 3.3. Calculation of available capital, TSCR, and OCR:

#### Additional information

	Item	Amount, euro, or indicator, %
<b>Total risk exposure amount (TREA), euro</b> (EU regulation No. 680/2014 report "C 02.00 — OWN FUNDS REQUIREMENTS (CA2)" row 010.)	<b>6.</b>	368 342 401
<b>Individual minimum capital adequacy indicator, %</b>	<b>7.</b>	11.20
<b>Overall capital ratio, %, incl.:</b> (EU regulation No. 680/2014 report "C 03.00 — CAPITAL RATIOS (CA3)" row 050.)	<b>8.</b>	21.04
CET1 Capital ratio, % (EU regulation No. 680/2014 report "C 03.00 — CAPITAL RATIOS (CA3)" row 010.)	8.1.	15.56
T1 Capital ratio, % (EU regulation No. 680/2014 report "C 03.00 — CAPITAL RATIOS (CA3)" row 030.)	8.2.	15.56

#### Capital available to the credit institution

	Item	Amount, euro, or indicator, %
<b>Total (9.1.+9.2.+9.3.), incl.:</b> (EU regulation No. 680/2014 report "C 01.00 — OWN FUNDS (CA1)" row 010.)	<b>9.</b>	<b>77 504 625</b>
common equity tier 1 capital (EU regulation No. 680/2014 report "C 01.00 — OWN FUNDS (CA1)" row 020.)	9.1.	57 303 985
additional tier 1 capital (EU regulation No. 680/2014 report "C 01.00 — OWN FUNDS (CA1)" row 530.)	9.2.	-
tier 2 capital (EU regulation No. 680/2014 report "C 01.00 — OWN FUNDS (CA1)" row 750.)	9.3.	20 200 640

#### TSCR calculation and adherence

	Item	Amount, euro
<b>TSCR amount (1.+2.-3.), incl.:</b>	<b>10.</b>	<b>41 254 349</b>
minimum tier 1 equity capital ratio requirement ( $\text{round}(\text{if}(9.3.>0;10.-\text{min}(10.*0.25;9.3.);10.);0)$ )	10.1.	30 940 761
<b>Capital surplus or deficit (9.-10.), incl.:</b>	<b>11.</b>	<b>36 250 276</b>
tier 1 equity capital (9.1.-10.1.)	11.1.	26 363 224

#### TSCR calculation and adherence

	Item	Indicator, %
<b>TSCR indicator</b> ( $\text{round}(8\%*(10.*12.5/6)*100;2)$ ), incl.:	<b>12.</b>	<b>11.2</b>
minimum tier 1 equity capital ratio requirement ( $\text{round}(8\%*(10.1.*12.5/6)*100;2)$ )	12.1.	8.4
<b>Capital surplus or deficit (round(11./6.*100;2), incl.:</b>	<b>13.</b>	<b>9.84</b>
tier 1 equity capital ( $\text{round}(11.1./6.*100;2)$ )	13.1.	7.16

#### OCR calculation and adherence

	Item	Amount, euro
<b>OCR amount (10.+4.+5.), incl.:</b>	<b>14.</b>	<b>50 647 080</b>
minimum requirement for tier 1 equity capital (10.1.+4.+5.)	14.1.	40 333 492
<b>Capital surplus or deficit (9.-14.), incl.:</b>	<b>15.</b>	<b>26 857 545</b>
tier 1 equity capital (9.1.-14.1.)	15.1.	16 970 493

## OCR calculation and adherence

	Item	Indicator, %
<b>OCR indicator</b> <i>(round(12.+4.*100/6.+5.*100/6.;2), incl:</i>	<b>16.</b>	<b>13.75</b>
<i>minimum tier 1 equity capital ratio requirement</i> <i>(round(12.1.+ 4.*100/6+5.*100/6.;2)</i>	16.1.	10.95
<b>Capital surplus or deficit</b> <i>(round(15./6.*100;2)), incl.:</i>	<b>17.</b>	<b>7.29</b>
tier 1 equity capital <i>(round(15.1./6.*100;2)</i>	17.1.	4.61

The overall capital reserve requirement (TCRR) as at 31.12.2016 was EUR 9.4 mio. The amount is obtained as the total of the capital maintenance reserve and the countercyclical capital reserve. The capital preservation reserve requirement equals 2.5% of the amount of risk-weighted assets, while the countercyclical reserve requirement is calculated as 0.05% of risk-weighted assets.

3.4. Calculation of the regulatory countercyclical capital reserve specific to the credit institution as at 31.12.2016:

Country	Risk-bearing transaction (RT) risk-weighted value	RT with support factor (RSV)	Risk-bearing transaction risk-weighted value with RSV	Equity capital requirement (*8%)	Equity capital requirement weightings	Countercyclical capital reserve baseline	
Sweden	344		344	28	0.00%	1.50%	0.41
Hong Kong	12,935,361	20,317	12,930,524	1,034,442	5.14%	0.625%	6 465.26
Norway	2,655,790		2,655,790	212,463	1.06%	1.50%	3 186.95

**Countercyclical capital reserve specific to the credit institution**

**0.04798%**

- 3.5. As at 31.12.2016, the Bank's available capital was calculated as EUR 77.5 mio., including EUR 57.3 mio. tier 1 equity capital and EUR 20.2 mio. tier 2 capital.
- 3.6. TSCR volume and indicator calculation as at 31.12.2016: TSCR volume – EUR 41.3 mio., corresponding to the minimum tier 1 equity capital of EUR 30.9 mio. TSCR indicators – 11.2% and 8.4% respectively. TSCR volume calculation indicates a capital surplus of EUR 36.3, including tier 1 equity capital surplus of EUR 26.4 mio.
- 3.7. OCR volume and indicator calculation as at 31.12.2016: OCR volume – EUR 50.7 mio., corresponding to the minimum tier 1 equity capital of EUR 40.3 mio.. OCR indicators – 13.75% and 10.95% respectively. OCR volume calculation indicates a capital surplus of EUR 26.9 mio., with tier 1 equity capital surplus of EUR 16.97 mio.
- 3.8. Within the framework of its capital planning process, the Bank includes the option of increasing tier 1 capital in case of necessity, by converting part of the tier 2 capital invested by Bank shareholders to tier 1 equity capital.