



Baltic International Bank

BUSINESS REVIEW
2016

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VALERI BELOKON,
CHAIRMAN OF THE
SUPERVISORY BOARD

The best way to predict the future, is to create it yourself. It is a constant and unchanging truth over ages, and we, Baltic International Bank, believe that by purposeful and well-considered work today we can create a future where we wish to live ourselves and hope to leave to our children and grandchildren.

Looking into future, Baltic International Bank started to implement the new strategy of the Bank for the period until 2030, and the entire strategy is focused on sustainable investments. Our goal is to invest in perspective projects and environmentally friendly technologies together with our clients, thus contributing both to profitable passing down the wealth of our clients to next generations and – to sustainable development of the entire world.

Year 2017 will be special in the life of Baltic International Bank – we will celebrate the 25th anniversary of the Bank. I am pleased that at the eve of the anniversary we have become even more strong, experienced and farsighted bank. We are proud to create future together with you!

Valeri Belokon,
Chairman
of the Supervisory Board





ILONA GULCHAK,
THE CHAIRPERSON OF THE
MANAGEMENT BOARD

Currently, the financial services industry in Latvia and worldwide undergoes sizeable changes. Digitisation, data security, ever-growing regulatory requirements and ever-changing financial needs of customers is only a part of the challenges that we must be ready to tackle already today. Based on the belief that challenges posed by ever-changing market fuel however further growth, Baltic International Bank continued its sustainable development in 2016 and hence laid down a stable and well-thought-out anchor for the next phase of Bank's business.

In 2016, Bank articulated its new Strategy 2030 (Bank embarked on developing the strategy in 2015) which centres around and places the main focus on environmentally friendly investments. The paramount strategic goal is to invest jointly with the customers in the enterprises whose activities resonate with environmental, social and governance (ESG) factors. We strongly believe that the use of the newest technologies, production of renewable energy (use of alternative energy sources) and responsible use of natural resources represents not only a source of steady profit but also underlie prospective entrepreneurship. ESG-based investment solutions therefore shape our responsible choice, and our customers start appreciating the choice as well. They employ our offers for partial diversification of their aggregate asset portfolio or intend to use Bank-constructed bespoke investment portfolios having a built-in ESG component.

While embarking on the active implementation of Bank's operational strategy geared towards sustainable investments, in 2016 Bank invested a substantial amount in Germany-based Green Gateway Fund. Under the new strategic approach, Baltic International Bank designed new ESG-compliant investment offerings and products in 2016.

At the end of 2016, Baltic International Bank established its new subsidiary AS „BIB Alternative Investment Management”. The subsidiary will manage alternative investment funds and will provide investors with the opportunity of investing in business projects which are underpinned by new technologies and foster the efficient use of natural resources.

In 2016, Baltic International Bank placed a special focus on enhancing the efficiency and effectiveness of its internal control system. Bank made sizeable investments in the information technologies infrastructure and implemented a number of software solutions to enable Bank to better manage compliance risk, automate business processes, and maximally ensure data security.

We firmly believe that our refocus on the new business model will provide a solid basis for further sustainable growth of Baltic International Bank.

I wish to heartily thank our customers, partners and shareholders for cooperation, in-depth understanding of the ongoing changes, and support. I would like to deliver special thanks to our staff members for their personal endurance, high-level professionalism, and dedication and love towards work.

Ilona Gulchak
The Chairperson
of the Management Board



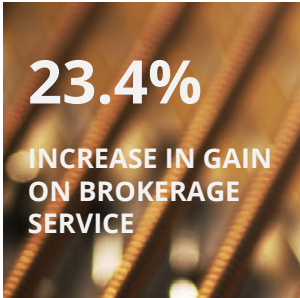


EUR 444 MILLION

CUSTOMERS' FUNDS UNDER MANAGEMENT
(assets under management, portfolio of brokerage services, debt securities issued, deposits, subordinated deposits)

42.8%

INCREASE OF THE OPERATING INCOME



23.4%

INCREASE IN GAIN ON BROKERAGE SERVICE



403.02%

LIQUIDITY COVERAGE RATIO



EUR 8.57 MILLION

INCREASE OF THE VOLUME OF TRADING OPERATIONS

OVERVIEW OF FINANCIAL RESULTS OF THE BANK

In 2016, Baltic International Bank put a special emphasis on diversifying Bank's business activities and sources of profits, developing new offerings, improving asset quality, enhancing Bank's internal processes, and boosting operational efficiency.

At the end of December 2016, Baltic International Bank **revenue from core operations** reached EUR 28.25 million, which is a 42.8% increase over the same period a year ago. The positive dynamics of core operations' revenue were mostly facilitated by trade transactions, where revenue increased by EUR 8.57 million. During 2016, the Bank's revenues from brokerage transactions also grew significantly – by 23.4% as compared to the beginning of the year. Income from transactions and administration of current accounts and investment accounts grew by 2.36 percent in 2016, thus indicating on a gradual diversification of the sources of fee and commission income.

The amount of **assets** held by Baltic International Bank at the end of December 2016 reached EUR 308.4 million, dominantly represented by investments in available-for-sale financial assets: EUR 85.75 million or 27.83 percent of the total assets. High quality liquid assets (assets carrying investment-grade credit ratings and balances due from the Bank of Latvia) totalled EUR 162.55 million or 52.7 percent of the total assets. Investments in government bonds totalled EUR 47.09 million or 15.43 percent of the total assets

Assets under management reached EUR 81.98 million. The value of financial instruments in brokerage service totalled EUR 105.67 million. **Total clients' funds** under management at the end of the year amounted to EUR 444 million.

The Bank's **liquidity indicators** surpass the minimum requirements – at the end of December 2016, the Bank's liquidity ratio was 70.01% (minimum internal requirement: 60%). The liquidity coverage ratio was 404,06%, which significantly exceeds the 2016 requirement of 70%. Net stable funding ratio (NFSR), which demonstrates a sustainable funding structure, has reached 143.40% exceeding the regulating requirement, which has been set at 100% and will come into force in 2018.

As of 31 December 2016, the Bank's own funds totalled EUR 33.7 million. The Bank's Tier I capital ratio (CETI) totalled 12.62 percent. Having reached 16.48 percent, the total capital ratio exceeds the individual ratio, as set by the Financial and Capital Market Commission, by 6.28 percentage points. By the end of 4Q 2016, the leverage ratio was 8.35 percent.



BANK AND SOCIETY

Baltic International Bank continued to support culture, arts, sports, science and entrepreneurial projects being significant to the community of Latvia during 2016.

LITERATURE AND ARTS

Latvian **literature** development is one of the long-standing areas of the Bank's focus within the framework of social support. We are proud of the fact that among the books supported by the Bank there are a lot of publications of great importance for Latvia's literature and history of culture.

We believe that knowledge of culture and history of one's country is the basis of the national identity of each nation. For this very reason, Baltic International Bank is glad to render support to the historical novel series "We. Latvia. The 20th Century", and several works were published in the series in 2016. The Bank continued to support the Annual Latvian Literature Award (LaLiGaBa) in 2016 as well.

In 2016 the bank supported several outstanding **art** projects. As a result of cooperation between the Latvian National Art Museum (the 'LNAAM') and the Bank, a mobile application of the LNMA, being one of the most advanced museum applications, was developed. We are proud the mobile application supported by the Bank enables each visitor of the museum to see the exhibition and architecture of the unique building paying attention to details and nuances that hide exciting stories and new levels of cognition.

In 2016, under the Bank's support, guest performance of the world's most famous male ballet dancer Mikhail Baryshnikov was held in Latvian National Opera with a one-man show Letter to a Man.

SCIENCE AND ENTREPRENEURSHIP

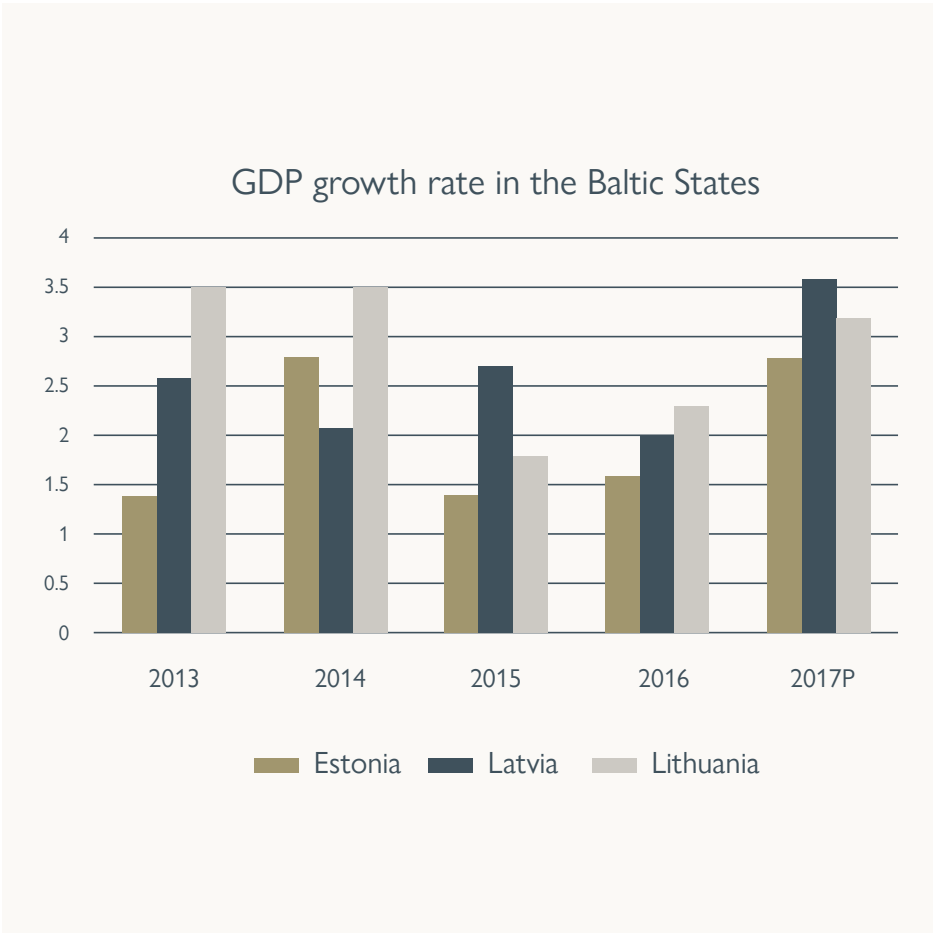
Baltic International Bank has for several years been supporting the platform for the creation of new businesses "**Commercialization Reactor**". This international technology commercialisation platform was developed in Latvia with the aim to combine scientific excellence with entrepreneurial experience and knowledge thus creating the basis for the development and activity of new and successful high tech companies. Expanding cooperation with start-ups, Baltic International Bank started cooperating with the Latvian Start-up Association StartIn.

We are proud that the "**Baltic International Bank's Latvian Barometer**" – a monthly public opinion survey on the public opinion concerning various social and economic issues – is being published with the support of the Bank. This project is valuable and interesting both to state and governmental institutions, academics and students, business people and wide society.

ENVIRONMENT AND SUSTAINABILITY

Baltic International Bank started focusing on ESG (Environmental. Social. Governance) approach in 2016. Both in everyday operations, as well as analysis and implementation of investment and financing projects the Bank takes care of the environment and its protection.

We are pleased that participating in the Sustainability Index organised by the Institute for Corporate Sustainability and Responsibility, Employers' Confederation of Latvia and Free Trade Union Confederation of Latvia, in 2016 the Bank was awarded the Silver Prize!



ECONOMIC OVERVIEW OF LATVIA AND THE BALTIC STATES

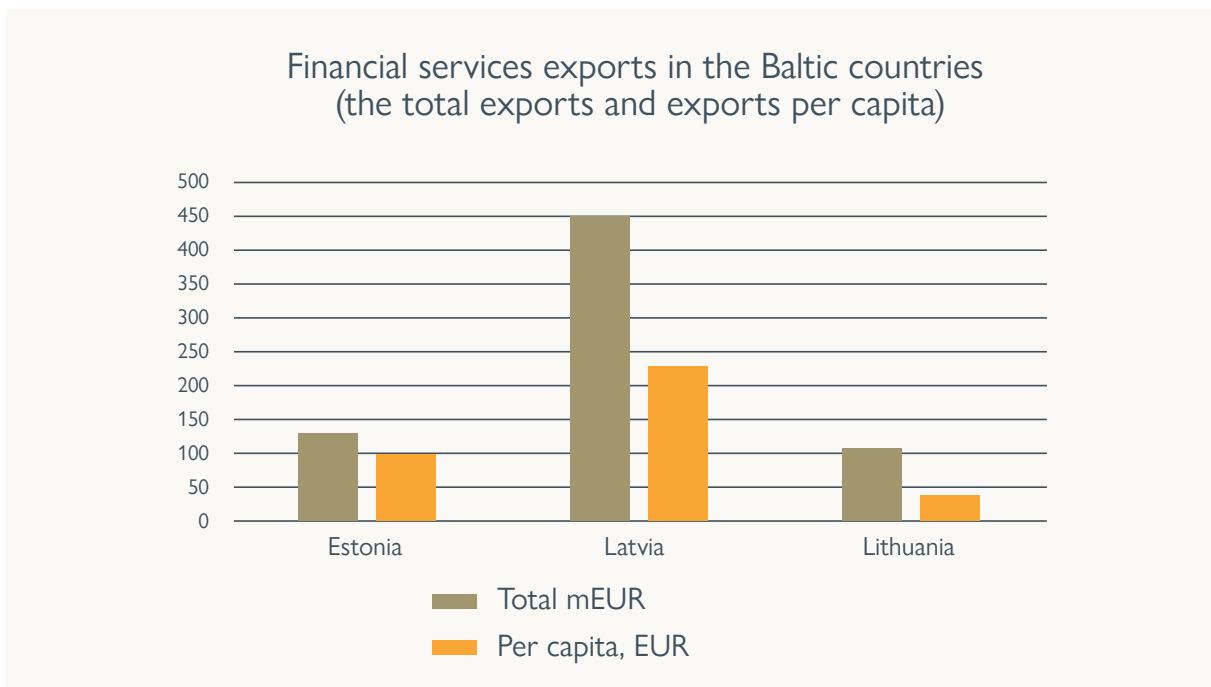
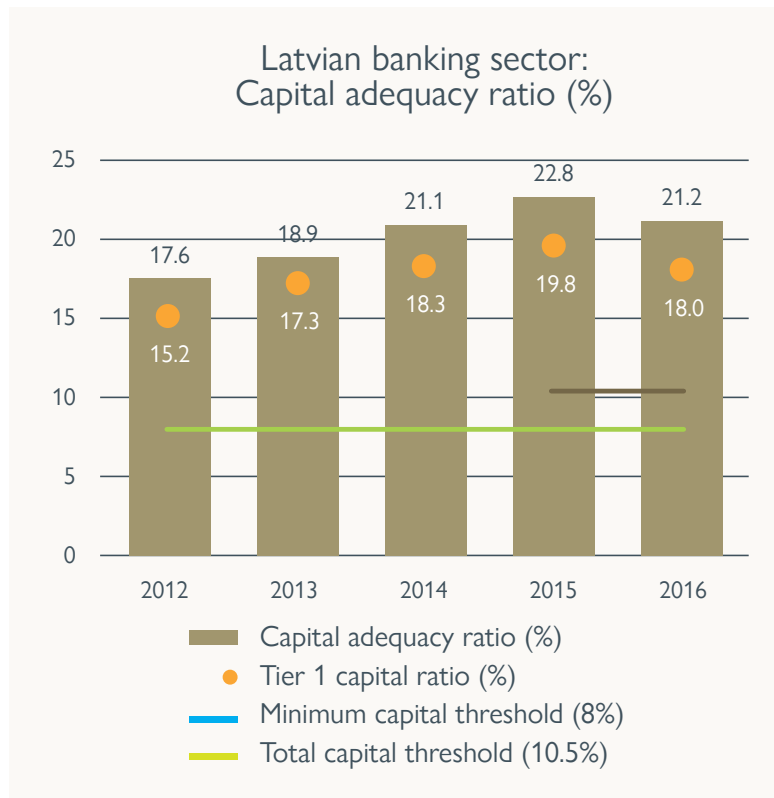
ECONOMY OF LATVIA IN 2016

Latvia's gross domestic product (GDP) slowed, compared to a 2.7-percent growth in 2015, and stood at 2.0% in 2016. The country's economy was adversely affected by failure to absorb the structural funds from the EU budget and by a decrease in the volume of foreign direct investments (FDI). Unlike previous years – when the volume of the acquired FDI in Latvia surged, albeit slightly (2014: EUR 150 million; 2015: EUR 190 million) – the volume of the acquired FDI dropped by EUR 211.6 million in 2016. Thus, the 2017 priorities set by the government of the Republic of Latvia and by other stakeholders include the acquisition of FDI and unlocking the full potential of EU structural funds.

In 2016, the manufacturing sector contributed largely to the country's economic growth and increased the level of value added by 5.6%. Overall, the trading sector represents a slightly larger segment since an export-oriented wholesale in Latvia plays a significant role. The sector grew at a slow but tangible pace (3.3%) and exceeded the average growth rate.

As the numbers of the tourist flow grew substantially, the HoReCa industry in Latvia turned out to be the most fast growing one. Growth of the software and information services industry exceeded even the 30-percent mark last year. Largely due to this fact, export of services not related to transit soared by one-tenth last year and hence contributed nearly EUR 300 million to the total income. Construction volumes slid by 18% in 2016.

In 2016, Latvia's banking sector continued to develop gradually. The aggregate lending volume is showing growth already for a second consecutive year. During the year, the sector-wide loan portfolio went up by 3.1% to reach EUR 15.1 billion. During the period, the participants of Latvia's banking sector continued to revise customers' portfolios. Thus, the sector witnessed a decline in customer deposits and in the aggregate assets. A positive signal is that the sector-wide ROA and ROE exceed the average figures of the EU Member States. The sector's cost-to-sales-revenue ratio, often referred to as the efficiency ratio, is one of the best ratios across the EU. The sector-wide capital adequacy and liquidity ratios by far exceed the minimum regulatory thresholds.



ECONOMIES OF THE BALTIC STATES IN 2016

Economic growth in the Baltic States predominantly relies on exports. Structural changes (a shift in the basic ways an economy operates) are the main driver of a growth. Although the structural changes occur on a going basis, they are hardly visible in everyday life. However, occasionally it becomes clear that the economy somehow acquires another quality.

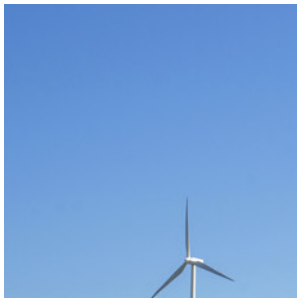
In the three Baltic countries, the timber processing and food stuff sectors were traditionally important. In Lithuania, the chemical sector and the downstream sector (the refining of crude oil) play a great role. Of the three countries, Estonia was the first that succeeded to strengthen the electronics industry and machinery industry. In the first decade of the 21st century, exports of goods continued to evolve both qualitatively and quantitatively, and it got sharply diversified. Industries such as machinery, electronics, and pharmaceutical became of paramount importance. In this decade, high value-added export of services is becoming more and more a vector for economic growth. In the three Baltic countries, the category of those services comprises business-specific outsourcing services. Software and communication services are also important, especially in Latvia and Estonia. Latvia is the leader in financial services exports.

FORECASTS FOR 2017

According to our forecast, Latvia is likely to become the fastest growing economy among the Baltic countries in the next few years. Estonia's economy is expected to develop at the slowest pace. Deep-seated economic reforms carried out by Estonian government will bring economic gains, albeit later. In the foreseeable future, the country's ability to fulfil its unexploited economic potential on business-cycle level will produce a drastic impact. The highest rate of employment and the sluggish wage rise in Latvia point to extremely unexploited economic potential. It is therefore imperative that the county accelerates its economic growth rate. It is quite clear that Estonia is close to full employment which in the Baltic States stands at nearly 5%, and the wage growth exceeding productivity growth for a number of years is a testimony to the fact. Largely due to its superb educational system and effective governance, Estonia has good perspectives for accelerating its economic growth steadily during the reporting period and for outperforming other Baltic States in the future.

We anticipate that 2017 in Latvia will be a successful year for the manufacturing and other exporting sectors, except for transit. Investments in Latvia's economy or gross fixed capital formation as a share of GDP, including investments in machinery and equipment (M&E), surpass the EU average. EU structural funds are used for fostering development of business clusters, investments in research and development (R&D), new product development (NPD). And those activities are expected to bring benefit, albeit gradually. It is also likely that the worst-hit construction sector will grow robustly in 2017 and is poised to remain at a peak throughout many years. Factors that may contribute to the sector's growth include the absorption of ES funds, housing construction, and the implementation of the RailBaltica project (a project to link Finland, the Baltic States and Poland with a standard gauge rail line).

In 2017 and beyond, development of Latvia's economy may be considerably affected by the country's tax policy changes envisaged by the Latvian government in their effort to enhance investments, boost economic activity rate (EAR), increase the volume of investments geared towards development of already operating businesses and of newly-established businesses (start-ups) in Latvia.



1.7
GIGATONNES

PREVENTED
EMISSION OF CO₂
IN 2016 BY USAGE
OF RENEWABLE
ENERGY



113.7
BILLION USD

NEW INVESTMENT IN
SOLAR ENERGY IN 2016



11.3%

GLOBAL
ELECTRICITY FROM
RENEWABLE
SOURCES IN 2016

112.5
BILLION USD

NEW INVESTMENT
IN WIND ENERGY
IN 2016

ESG INVESTMENT TRENDS

As non-renewable energy sources globally decline, the production of renewable energy sources is rapidly developing worldwide. The total amount of new investment in the production of renewable energy worldwide in 2015 reached 286 billion USD. The story of renewable energy in 2016 can be described as “more for less” – there was record installation of renewable power capacity worldwide in 2016, nevertheless the global new investment in renewable decreased. Wind, solar, biomass and waste-to-energy, geothermal, small hydro and marine sources between them added 138.5GW, up from 127.5GW in the previous year. In 2016 for the fifth successful year the investment in production of renewable energy was practically double than in fossil fuel. The proportion of global electricity coming from these renewable sources increased from 10.3% in 2015 to 11.3% in 2016. It prevented the emission of an estimated 1.7 gigatonnes of CO₂.*

Speaking on the decrease of global investment amounts in renewable, it was based on two main reasons. One of them was lower costs of the photovoltaic, onshore wind and offshore wind technologies, and the other one – a marked slowdown in financing amounts in China, Japan and some emerging markets during the year.

The amounts of production of renewable energy will increase in the further years and decades as well, and we are pleased that while investing in environmentally friendly and sustainable projects, Baltic International Bank can provide its clients the opportunity not only to generate capital gains and pass their wealth down to the next generations, as well as makes a substantial and positive contribution to the development of the community and the world now and in the future.

* Data source: *Global Trends In Renewable Energy Investment 2017 (FS-UNEP Collaborating Centre for Climate & Sustainable Energy Finance, 2017)*

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