

CONFORMED COPY

LOAN NUMBER 7797 LV

Loan Agreement

(Financial Sector Development Policy Loan)

between

REPUBLIC OF LATVIA

and

**INTERNATIONAL BANK FOR RECONSTRUCTION
AND DEVELOPMENT**

Dated September 24, 2009

LOAN AGREEMENT

Agreement dated September 24, 2009, entered into the between REPUBLIC OF LATVIA (“Borrower”) and the INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (“Bank”) for the purpose of providing financing in support of the Program (as defined in the Appendix to this Agreement). The Bank has decided to provide this financing on the basis, *inter alia*, of: (a) the actions which the Borrower has already taken under the Program and which are described in Section I of Schedule 1 to this Agreement; and (b) the Borrower’s maintenance of an appropriate macro-economic policy framework. The Borrower and the Bank therefore hereby agree as follows:

ARTICLE I - GENERAL CONDITIONS; DEFINITIONS

- 1.01. The General Conditions (as defined in the Appendix to this Agreement) constitute an integral part of this Agreement.
- 1.02. Unless the context requires otherwise, the capitalized terms used in this Agreement have the meanings ascribed to them in the General Conditions or in the Appendix to this Agreement.

ARTICLE II - LOAN

- 2.01. The Bank agrees to lend to the Borrower, on the terms and conditions set forth or referred to in this Agreement, the amount of two hundred million Euro (EUR 200,000,000), as such amount may be converted from time to time through a Currency Conversion in accordance with the provisions of Section 2.07 of this Agreement (“Loan”).
- 2.02. The Borrower may withdraw the proceeds of the Loan in support of the Program in accordance with Section II of Schedule 1 to this Agreement.
- 2.03. The Front-end Fee payable by the Borrower shall be equal to one percent (1%) of the Loan amount.
- 2.04. The interest payable by the Borrower for each Interest Period shall be at a rate equal to LIBOR for the Loan Currency plus the Fixed Spread; provided, that upon a Conversion of all or any portion of the principal amount of the Loan, the interest payable by the Borrower during the Conversion Period on such amount shall be determined in accordance with the relevant provisions of Article IV of the General Conditions. Notwithstanding the foregoing, if any amount of the Withdrawn Loan Balance remains unpaid when due and such non-payment

continues for a period of thirty (30) days, then the interest payable by the Borrower shall instead be calculated as provided in Section 3.02 (d) of the General Conditions.

- 2.05. The Payment Dates are January 15 and July 15 in each year.
- 2.06. The principal amount of the Loan shall be repaid in accordance with the amortization schedule set forth in Schedule 2 to this Agreement.
- 2.07. (a) The Borrower may at any time request any of the following Conversions of the terms of the Loan in order to facilitate prudent debt management: (i) a change of the Loan Currency of all or any portion of the principal amount of the Loan, withdrawn or unwithdrawn, to an Approved Currency; (ii) a change of the interest rate basis applicable to all or any portion of the principal amount of the Loan withdrawn and outstanding from a Variable Rate to a Fixed Rate, or vice versa; and (iii) the setting of limits on the Variable Rate applicable to all or any portion of the principal amount of the Loan withdrawn and outstanding by the establishment of an Interest Rate Cap or Interest Rate Collar on the Variable Rate.
- (b) Any conversion requested pursuant to paragraph (a) of this Section that is accepted by the Bank shall be considered a "Conversion", as defined in the General Conditions, and shall be effected in accordance with the provisions of Article IV of the General Conditions and of the Conversion Guidelines.
- (c) Promptly following the Execution Date for an Interest Rate Cap or Interest Rate Collar for which the Borrower has requested that the premium be paid out of the proceeds of the Loan, the Bank shall, on behalf of the Borrower, withdraw from the Loan Account and pay to itself the amounts required to pay any premium payable in accordance with Section 4.05 (c) of the General Conditions up to the amount allocated from time to time for the purpose in the table in Section IV of Schedule 2 to this Agreement.
- 2.08. Without limitation upon the provisions of Section 5.08 of the General Conditions (renumbered as such pursuant to paragraph 4 of Section II of the Appendix to this Agreement and relating to Cooperation and Consultation), the Borrower shall promptly furnish to the Bank such information relating to the provisions of this Article II as the Bank may, from time to time, reasonably request.

ARTICLE III - PROGRAM

- 3.01 The Borrower declares its commitment to the Program and its implementation. To this end, and further to Section 5.08 of the General Conditions:
- (a) the Borrower and the Bank shall from time to time, at the request of either party, exchange views on the progress achieved in carrying out the Program;
 - (b) prior to each such exchange of views, the Borrower shall furnish to the Bank for its review and comment a report on the progress achieved in carrying out the Program, in such detail as the Bank shall reasonably request; and
 - (c) without limitation upon the provisions of paragraphs (a) and (b) of this Section, the Borrower shall promptly inform the Bank of any situation that would have the effect of materially reversing the objectives of the Program or any action taken under the Program, including any action specified in Section I.A of Schedule 1 to this Agreement.

ARTICLE IV - REMEDIES OF THE BANK

- 4.01. The Additional Events of Suspension consist of the following, namely, that a situation has arisen which shall make it improbable that the Program, or a significant part of it, will be carried out.

ARTICLE V - TERMINATION

- 5.01. The Effectiveness Deadline is the date ninety (90) days after the date of this Agreement.

ARTICLE VI - REPRESENTATIVE; ADDRESSES

- 6.01. The Borrower's Representative is the Minister of Finance.

- 6.02. The Borrower's Address is:

Smilšu 1,
Riga, LV-1919
Republic of Latvia

Facsimile:

+371 67095503

6.03. The Bank's Address is:

International Bank for Reconstruction
and Development
1818 H Street, N.W.
Washington, D.C. 20433
United States of America

Cable address:	Telex:	Facsimile:
INTBAFRAD Washington, D.C.	248423(MCI) or 64145(MCI)	1-202-477-6391

AGREED at Washington, DC, United States of America, as of the day and year first
above written.

REPUBLIC OF LATVIA

By: /s/ Andrejs Pildegovics

Authorized Representative

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

By: /s/ Theodore Ahlers

Authorized Representative

SCHEDULE 1**Program Actions; Availability of Loan Proceeds****Section I. Actions under the Program**

Actions Taken Under the Program. The actions taken by the Borrower under the Program include the following:

1. The BoL, with inputs from the FCMC, has completed stress tests of the banking sector in order to assess its resilience to potential worst case scenarios.
2. The Borrower has prepared a Strategic Contingency Plan for the financial sector on the basis of the results of the stress tests referred to in paragraph 1 above.
3. The Borrower's Parliament has approved amendments to the Credit Institution Law with a view to strengthen the Borrower's legal framework for bank resolution.
4. The Borrower's Parliament has approved amendments to the Insolvency Law with a view to: (i) removing potential obstacles to out-of-court proceedings for corporate restructuring; (ii) allowing pre-packaged restructuring agreements; and (iii) introducing further flexibility and easier access to insolvency proceedings.
5. The Borrower's Parliament has approved amendments to the Civil Procedure Law in order to simplify the existing mortgage foreclosure process.
6. The Borrower has implemented a debt restructuring program entailing: (i) the approval by the Consultative Council of guidelines for corporate debt restructuring and their publication by the Ministry of Justice; and (ii) the approval and publication by the FCMC of guidelines on mortgage debt restructuring.
7. The BoL has adopted an improved stress testing framework based on multiple scenarios and a revised credit risks module to be operated on a regular basis.
8. The FCMC has adopted a remedial action framework that establishes a matrix of triggers and a range of discretionary and non-discretionary supervisory actions for use when a bank has not complied with the laws, regulations and supervisory decisions.
9. The FCMC has: (i) issued revised and strengthened prudential regulations for asset quality and capital adequacy; (ii) prepared a draft liquidity risk management regulation to be revised on the basis of the recommendations of the Committee of European Banking Supervisors and the directives of the European Union; and

(iii) included the issuance of regulations on credit risk management in its action plan for 2009.

10. The Borrower has completed a comprehensive review of consumer protection laws, regulations and institutional set-up for the financial sector in line with international good practices.

Section II. Availability of Loan Proceeds

- A. General.** The Borrower may withdraw the proceeds of the Loan in accordance with the provisions of this Section and such additional instructions as the Bank may specify by notice to the Borrower.
- B. Allocation of Loan Amounts.** The Loan (except for amounts required to pay the Front-end Fee) shall be withdrawn in a single tranche. The allocation of the amounts of the Loan to this end is set out in the table below:

Allocations	Amount of the Loan Tranche Allocated (Expressed in Euro)
Single Tranche	198,000,000
Front-end Fee	2,000,000
Amount payable pursuant to Section 2.07(c) of this Agreement	0
TOTAL AMOUNT	<u>200,000,000</u>

- C. Deposits of Loan Amounts.** Except as the Bank may otherwise agree:
1. all withdrawals from the Loan Account shall be deposited by the Bank into an account designated by the Borrower and acceptable to the Bank; and
 2. the Borrower shall ensure that upon each deposit of an amount of the Loan into this account, an equivalent amount is accounted for in the Borrower's budget management system, in a manner acceptable to the Bank.

- D. Excluded Expenditures.** The Borrower undertakes that the proceeds of the Loan shall not be used to finance Excluded Expenditures. If the Bank determines at any time that an amount of the Loan was used to make a payment for an Excluded Expenditure, the Borrower shall, promptly upon notice from the Bank, refund an amount equal to the amount of such payment to the Bank. Amounts refunded to the Bank upon such request shall be cancelled.
- E. Closing Date.** The Closing Date is March 24, 2010.

SCHEDULE 2

Amortization Schedule

1. The following table sets forth the Principal Payment Dates of the Loan and the percentage of the total principal amount of the Loan payable on each Principal Payment Date (“Installment Share”). If the proceeds of the Loan have been fully withdrawn as of the first Principal Payment Date, the principal amount of the Loan repayable by the Borrower on each Principal Payment Date shall be determined by the Bank by multiplying: (a) Withdrawn Loan Balance as of the first Principal Payment Date; by (b) the Installment Share for each Principal Payment Date, such repayable amount to be adjusted, as necessary, to deduct any amounts referred to in paragraph 4 of this Schedule, to which a Currency Conversion applies.

Principal Payment Date	Installment Share (Expressed as a Percentage)
On each January 15 and July 15 beginning January 15, 2015 through July 15, 2019	10%

2. If the proceeds of the Loan have not been fully withdrawn as of the first Principal Payment Date, the principal amount of the Loan repayable by the Borrower on each Principal Payment Date shall be determined as follows:
- (a) To the extent that any proceeds of the Loan have been withdrawn as of the first Principal Payment Date, the Borrower shall repay the Withdrawn Loan Balance as of such date in accordance with paragraph 1 of this Schedule.
 - (b) Any amount withdrawn after the first Principal Payment Date shall be repaid on each Principal Payment Date falling after the date of such withdrawal in amounts determined by the Bank by multiplying the amount of each such withdrawal by a fraction, the numerator of which is the original Installment Share specified in the table in paragraph 1 of this Schedule for said Principal Payment Date (“Original Installment Share”) and the denominator of which is the sum of all remaining Original Installment Shares for Principal Payment Dates falling on or after such date, such amounts repayable to be adjusted, as necessary, to deduct any amounts referred to in paragraph 4 of this Schedule, to which a Currency Conversion applies.

3. (a) Amounts of the Loan withdrawn within two calendar months prior to any Principal Payment Date shall, for the purposes solely of calculating the principal amounts payable on any Principal Payment Date, be treated as withdrawn and outstanding on the second Principal Payment Date following the date of withdrawal and shall be repayable on each Principal Payment Date commencing with the second Principal Payment Date following the date of withdrawal.
 - (b) Notwithstanding the provisions of sub-paragraph (a) of this paragraph, if at any time the Bank adopts a due date billing system under which invoices are issued on or after the respective Principal Payment Date, the provisions of such sub-paragraph shall no longer apply to any withdrawals made after the adoption of such billing system.
4. Notwithstanding the provisions of paragraphs 1 and 2 of this Schedule, upon a Currency Conversion of all or any portion of the Withdrawn Loan Balance to an Approved Currency, the amount so converted in the Approved Currency that is repayable on any Principal Payment Date occurring during the Conversion Period, shall be determined by the Bank by multiplying such amount in its currency of denomination immediately prior to the Conversion by either: (i) the exchange rate that reflects the amounts of principal in the Approved Currency payable by the Bank under the Currency Hedge Transaction relating to the Conversion; or (ii) if the Bank so determines in accordance with the Conversion Guidelines, the exchange rate component of the Screen Rate.

APPENDIX**Section I. Definitions**

1. “BoL” means the Bank of Latvia, the Borrower’s Central Bank.
2. “Civil Procedures Law” means the Borrower’s law, adopted on October 14, 1998, as amended from time to time, setting forth civil procedures in the courts of the Republic of Latvia, including execution of judgments.
3. “Committee of European Banking Supervisors” means the committee established by decision 2009/78/EC of the European Communities on January 23, 2009.
4. “Consultative Council” means the Borrower’s Council, chaired by the Minister of Justice of the Borrower, responsible for developing and implementing insolvency policy, both on a national level and at the level of the EU, and includes the Minister of Justice, the Minister of Economics, and representatives of the Ministry of Finance, the Association of Certified Insolvency Administrators, the Latvian Commercial Banks Association, the Employers’ Confederation of Latvia, and the Free Trade Union Confederation of Latvia.
5. “Credit Institution Law” means the Borrower’s law, adopted on October 5, 1995, as amended from time to time, setting forth the legal status of credit institutions, regulation of their operations, liability and supervision, as well as determining the rights, duties and liabilities of those persons set out under the said law.
6. “Excluded Expenditure” means any expenditure:
 - (a) for goods or services supplied under a contract which any national or international financing institution or agency other than the Bank or the Association has financed or agreed to finance, or which the Bank or the Association has financed or agreed to finance under another loan, credit, or grant;
 - (b) for goods included in the following groups or sub-groups of the Standard International Trade Classification, Revision 3 (SITC, Rev.3), published by the United Nations in Statistical Papers, Series M, No. 34/Rev.3 (1986) (the SITC), or any successor groups or subgroups under future revisions to the SITC, as designated by the Bank by notice to the Borrower:

Group	Sub-group	Description of Item
112		Alcoholic beverages
121		Tobacco, un-manufactured, tobacco refuse
122		Tobacco, manufactured (whether or not containing tobacco substitutes)
525		Radioactive and associated materials
667		Pearls, precious and semiprecious stones, unworked or worked
718	718.7	Nuclear reactors, and parts thereof; fuel elements (cartridges), non-irradiated, for nuclear reactors
728	728.43	Tobacco processing machinery
897	897.3	Jewelry of gold, silver or platinum group metals (except watches and watch cases) and goldsmiths' or silversmiths' wares (including set gems)
971		Gold, non-monetary (excluding gold ores and concentrates)

- (c) for goods intended for a military or paramilitary purpose or for luxury consumption;
- (d) for environmentally hazardous goods, the manufacture, use or import of which is prohibited under the laws of the Borrower or international agreements to which the Borrower is a party);
- (e) on account of any payment prohibited by a decision of the United Nations Security Council taken under Chapter VII of the Charter of the United Nations; and
- (f) with respect to which the Bank determines that corrupt, fraudulent, collusive or coercive practices were engaged in by representatives of the

Borrower or other recipient of the Loan proceeds, without the Borrower (or other such recipient) having taken timely and appropriate action satisfactory to the Bank to address such practices when they occur.

7. “FCMC” means the Borrower’s Financial and Capital Market Commission, the entity responsible for the regulation and supervision of the functioning of the financial and capital market and its participants.
8. “General Conditions” means the “International Bank for Reconstruction and Development General Conditions for Loans”, dated July 1, 2005 (as amended through February 12, 2008) with the modifications set forth in Section II of this Appendix.
9. “Insolvency Law” means the Borrower’s law, adopted on November 1, 2007, as amended from time to time, setting forth the principles necessary to facilitate solvency and to protect the interests of creditors in situations of limited debtor solvency or debtor insolvency.
10. “Program” means the program of actions, objectives and policies designed to promote growth and achieve sustainable reductions in poverty and to support the Borrower’s reforms in the financial sector to build a sound financial system able to absorb the effects of the crisis and the contraction of economic activity and to resist to potential future shocks, set forth or referred to in the letter dated July 20, 2009, from the Borrower to the Bank declaring the Borrower’s commitment to the execution of the Program, and requesting assistance from the Bank in support of the Program during its execution.
11. “Single Tranche” means the amount of the Loan allocated to the category entitled “Single Tranche” in the table set forth in Part B of Section II of Schedule 1 to this Agreement.
12. “Strategic Contingency Plan” means the plan setting forth: (i) a typology of potential actions and interventions by the FCMC, the BoL and the Ministry of Finance in response to potential liquidity or solvency problems in the banking sector; (ii) a strategy for the resolution of potentially illiquid or insolvent banks according to their systemic importance and other relevant parameters; (iii) clear responsibilities for the implementation of, and the communication about such strategy; and (iv) directions in the case of a systemic crisis.

Section II. Modifications to the General Conditions

The modifications to the General Conditions are as follows:

1. The last sentence of paragraph (a) of Section 2.03 (relating to Applications for Withdrawal) is deleted in its entirety.

2. Sections 2.04 (*Designated Accounts*) and 2.05 (*Eligible Expenditures*) are deleted in their entirety, and the remaining Sections in Article II are renumbered accordingly.
3. Paragraph (a) of Section 2.05 (renumbered as such pursuant to paragraph 2 above) is modified to read as follows:

“Section 2.05. Refinancing Preparation Advance; Capitalizing Front-end Fee and Interest

(a) If the Loan Agreement provides for the repayment out of the proceeds of the Loan of an advance made by the Bank or the Association (“Preparation Advance”), the Bank shall, on behalf of such Loan Party, withdraw from the Loan Account on or after the Effective Date the amount required to repay the withdrawn and outstanding balance of the advance as at the date of such withdrawal from the Loan Account and to pay all accrued and unpaid charges, if any, on the advance as at such date. The Bank shall pay the amount so withdrawn to itself or the Association, as the case may be, and shall cancel the remaining unwithdrawn amount of the advance.”

4. Sections 5.01 (*Project Execution Generally*), and 5.09 (*Financial Management; Financial Statements; Audits*) are deleted in their entirety, and the remaining Sections in Article V are renumbered accordingly.
5. Paragraph (a) of Section 5.05 (renumbered as such pursuant to paragraph 4 above and relating to *Use of Goods, Works and Services*) is deleted in its entirety.
6. Paragraph (c) of Section 5.06 (renumbered as such pursuant to paragraph 4 above) is modified to read as follows:

“Section 5.06. Plans; Documents; Records

... (c) The Borrower shall retain all records (contracts, orders, invoices, bills, receipts and other documents) evidencing expenditures under the Loan until two years after the Closing Date. The Borrower shall enable the Bank’s representatives to examine such records.”

7. Paragraph (c) of Section 5.07 (renumbered as such pursuant to paragraph 4 above) is modified to read as follows:

Section 5.07. Program Monitoring and Evaluation

... (c) The Borrower shall prepare, or cause to be prepared, and furnish to the Bank not later than six months after the Closing Date, a

report of such scope and in such detail as the Bank shall reasonably request, on the execution of the Program, the performance by the Loan Parties and the Bank of their respective obligations under the Legal Agreements and the accomplishment of the purposes of the Loan.

8. The following terms and definitions set forth in the Appendix are modified or deleted as follows, and the following new terms and definitions are added in alphabetical order to the Appendix as follows, with the terms being renumbered accordingly:

(a) The definition of the term “Conversion Date” is modified to read as follows:

“‘Conversion Date’ means, in respect of a Conversion, the Execution Date (as herein defined) or such other date as requested by the Borrower and accepted by the Bank, on which the Conversion enters into effect, and as further specified in the Conversion Guidelines.”

(b) The definition of the term “Eligible Expenditure” is modified to read as follows:

“‘Eligible Expenditure’ means any use to which the Loan is put in support of the Program, other than to finance expenditures excluded pursuant to the Loan Agreement.”

(c) The term “Financial Statements” and its definition are deleted in their entirety.

(d) The term “Fixed Spread” is modified to read as follows:

“‘Fixed Spread’ means two percent (2%) per annum; provided, that: (a) for purposes of determining the Default Interest Rate, pursuant to Section 3.02 (d), that is applicable to an amount of the Withdrawn Loan Balance on which interest is payable at a Fixed Rate, the “Fixed Spread” means the Bank’s fixed spread in effect at 12:01 a.m. Washington, D.C. time, one calendar day prior to the date of the Loan Agreement, for the Currency of denomination of such amount; and (b) upon a Currency Conversion of all or any amount of the Unwithdrawn Loan Balance pursuant to Section 4.04 (a), the Fixed Spread shall be adjusted on the Execution Date in the manner specified in the Conversion Guidelines.

- (e) The term “Project” is modified to read “Program” and its definition is modified to read as follows (and all references to “Project” throughout these General Conditions are deemed to be references to “Program”):

“‘Program’ means the program referred to in the Loan Agreement in support of which the Loan is made.”