AS LHV Varahaldus

Annual Report 2007

(Translation of the Estonian original)

Annual Report	**01.01.2007 - 31.12.2007**
Business Name	AS LHV Varahaldus
Commercial Registry No.	10572453
Legal address	Tartu mnt. 2, Tallinn 10145
Phone	(372) 6800400
Fax	(372) 6800402
Main activities	Fund management, EMTAK 66301 (Estonian version of NACE)
Management Board	Mihkel Oja
	Rain Lõhmus
	Rait Kondor
Supervisory Board	Andres Viisemann
	Liisi Ruus
	Erki Kilu
	Charles Smith
Auditor	AS PricewaterhouseCoopers

Table of contents

MANAGEMENT REPORT

AS LHV Varahaldus is a fund management company. In 2007 the main business activity of the company was to provide fund management services to five mandatory pension funds, one supplementary pension fund and two equity Eurofunds (UCITSs).

Among pension funds with progressive strategy (up to 50% of the assets are invested in equities) the best performing fund in 2007 was LHV New Markets Pension Fund, which was the only one to achieve double digit net return. The success of LHV New Markets was due to bigger allocation to Southeast Asia and Latin-America. The performance of LHV Global Equities Pension Fund, which invests proportionally more into developed industrial markets (Western Europe, USA, Japan), was lower, as return on stock markets in developed markets remained weaker or was even negative on some markets in 2007.

Progressive pension funds compared	NAV 31.12.2006	NAV 31.12.2007	Growth of the NAV
LHV New Markets PF	**13.62**	**15.07**	**10.65%**
SEB Ühispank PF Progressive	15.71	17.17	9.29%
Sampo Pension 50	14.96	16.05	7.29%
Ergo Future PF	15.73	16.64	5.79%
LHV Global Equities PF	**16.65**	**17.58**	**5.59%**
Hansa PF K3	16.07	16.96	5.54%

Among pension funds with balanced investment strategies (up to 25% of the assets are invested in equities) the highest return was achieved by LHV Balanced Strategy Pension Fund, which unit value went up 5.16% in year 2007. It was the third year in a row when LHV's fund achieved the best return within this category.

Balanced pension funds compared	NAV 31.12.2006	NAV 31.12.2007	Growth of the NAV
LHV Balanced Strategy PF	**12.41**	**13.05**	**5.16%**
Sampo Pension 25	12.97	13.55	4.47%
Hansa PF K2	13.45	14.05	4.46%

Although LHV's conservative pension funds (all assets are invested in fixed income instruments) have been on average best performing since the inception of pension system in Estonia, we did not take the first place in 2007. Partly lower return was due to small allocation to government bonds, which was one of very few asset classes to perform well in the second half of 2007, when credit crisis spread over financial markets. LHV is underweight in government bonds as the risk of rising risk free interest rates is high, especially as they are historically low and inflation is still a concern for the global economy.

Conservative pension funds compared	NAV 31.12.2006	NAV 31.12.2007	Growth of the NAV
Sampo Pension Interest	11.22	11.60	3.39%
Hansa PF K1	11.47	11.75	2.44%
LHV Dynamic Bonds PF	**12.56**	**12.78**	**1.75%**
Ergo Stable PF	11.49	11.65	1.39%
SEB Ühispank PF Conservative	11.24	11.38	1.25%
LHV Quality Bonds PF	**11.85**	**11.98**	**1.10%**

LHV Supplementary Pension Fund, which invests on average 75% of its portfolio on equity markets, raised the value by 7.68% during the last year. Higher proportion of equities enabled it to achieve a higher return in comparison with our II pillar progressive fund LHV Global Equities PF, however it underperformed our another II pillar fund LHV New Markets PF, as the equity related investments in the supplementary fund were more biased towards developed industrial markets, which underperformed in comparison with emerging markets.

Supplementary pension funds comparison	NAV 31.12.2006	NAV 31.12.2007	Growth of the NAV
SEB Ühispank PF Active (100)	16.40	18.58	13.34%
SEB Ühispank PF Balanced (35)	17.50	19.30	10.30%
Sampo Pension Fund (50)	17.47	19.08	9.20%
Hansa PF V3 (100)	21.23	23.06	8.62%
LHV Supplementary PF (75)	**17.18**	**18.50**	**7.68%**
Hansa PF V2 (60)	15.98	16.95	6.07%
Hansa PF V1 (30)	19.03	19.81	4.10%

Two equity Eurofunds (both UCITSs), which were founded in 2007, started their investment activities with a pretty bad timing taking into account what happened on global equity markets. Credit crisis, which emerged from US sub-prime problems, weighed down global equity markets during the second half of the year, whereas Eastern Europe, which is the target region for LHV Emerging Europe Alpha Fund, was one of the weakest by its return. The return of LHV World Equities Funds was positive last year due to investments into Asia and Latin-America.

LHV UCITS funds	NAV at the beginning	NAV 31.12.2007	Change in the NAV
LHV World Equities Fund	10.0000	10.3776	3.78%
LHV Emerging Europe Alpha Fund	10.0000	8.6648	-13.35%

In the end of 2007, the total amount of assets under management by LHV Varahaldus was 500 million kroons, out of which 89% was in mandatory pension funds. In the end of 2006 the total amount of the assets under management was 331 million kroons.

In 2008 the company plans to broaden its family of equity funds. In the first quarter of the year LHV Persian Gulf Fund was launched, which invests mostly in listed equities in GCC (Gulf Cooperation Council) countries, including Bahrain, Oman, Qatar, Kuwait, and United Arab Emirates. LHV Persian Gulf Fund sees growth and opportunities outside the energy sector and therefore invests in banking, insurance, infrastructure, communication, construction, and utility businesses.

In 2008 the objective of the company is to increase its market share in mandatory pension market and increase the volume of assets under management in its equity funds through positive returns as well as new investors.

As at 31.12.2007 the company had 7 employees (31.12.0006: 6 employees). During the reporting period the company paid a total of 2 195 510 kroons in salaries (2006: 994 752 kroons), out of which 522 045 kroons was paid to management board members (2006: 344 784 kroons). Supervisory board members did not receive any remuneration during the reporting period.

FINANCIAL STATEMENTS

Management Board's confirmation of the financial statements

The Management Board confirms the correctness and completeness of AS LHV Varahaldus 2007 financial statements as presented on pages 6-19.

The Management Board confirms that:

- the accounting policies used in preparing the financial statements are in compliance with the generally accepted accounting principles of Estonia;
- the financial statements present a true and fair view of the financial position, the results of operations and the cash flows of the Company;
- AS LHV Varahaldus is a going concern.

Mihkel Oja ....
Member of the Board

Rain Lõhmus ....
Member of the Board

Rait Kondor ....
Member of the Board

Tallinn, 07.04.2008

Balance Sheet

(in Estonian kroons)

Assets	Note	31.12.2007	31.12.2006
Current assets			
Cash and bank	2	1 470 083	19 157 073
Short term financial investments	3	15 270 420	3 005 716
Derivatives	4	0	254 152
Loans given	7	0	4 284 848
Other receivables	7	805 256	522 863
Accrued income		405 591	160 763
Other prepaid expenses		327 241	858 692
Total current assets		**18 278 591**	**28 244 107**
Non-current assets			
Units of managed pension funds	5	29 041 684	27 669 992
Units of managed investment funds	5	8 938 465	0
Property, plant and equipment	6	51 504	32 479
Intangible assets	6	1 196 576	1 200 455
Total non-current assets		**39 228 229**	**28 902 926**
Total assets		**57 506 820**	**57 147 033**
Liabilities and equity			
Current liabilities			
Derivatives	4	0	197 000
Supplier payables	7	759 694	725 873
Accrued expenses and other liabilities	8	442 322	256 087
Provisions	9	4 880 000	4 180 000
Total current liabilities		**6 082 016**	**5 358 960**
Equity			
Share capital	10	63 000 000	63 000 000
Share premium		4 100 000	4 100 000
Accumulated losses		-15 311 927	-9 158 143
Net loss for financial year		-363 269	-6 153 784
Total equity		**51 424 804**	**51 788 073**
Total liabilities and equity		**57 506 820**	**57 147 033**

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Initsiaalid/initials M. M
Kuupäev/date 07.04.08
PricewaterhouseCoopers, Tallinn

Income statement

(in Estonian kroons)	Note	2007	2006
Fee income	11	9 705 786	5 992 386
Other operating income		124 296	34 103
Total operating income		**9 830 082**	**6 026 489**
Operating expenses	7,12	-9 572 444	-12 472 035
Personnel expenses			
Wages and salaries		*-2 195 510*	*-994 752*
Social security costs		*-720 267*	*-376 171*
Unemployment insurance expense		*-5 456*	*-3 205*
Total personnel expenses		-2 921 233	-1 374 128
Depreciation and amortization	6	-35 326	-11 420
Provision expense	9	-700 000	-1 680 000
Other operating expenses		-67 152	-31 873
Total operating expenses		**-13 296 155**	**-15 569 456**
Operating loss		**-3 466 073**	**-9 542 967**
Financial income and expense			
Profit from revaluation of short-term securities		2 119 875	580 135
Profit from revaluation of units of managed funds	5	922 198	2 342 069
Other interest and dividend income		159 764	91 307
Profit from derivatives		0	568 999
Foreign exchange losses		-99 033	-193 327
Total financial income and expenses		**3 102 804**	**3 389 183**
Net loss for the financial year		**-363 269**	**-6 153 784**

Cash flow statement

(in Estonian kroons)	Note	2007	2006
Cash flow from operating activities			
Operating loss		-3 466 073	-9 542 967
Adjustments:			
Depreciation and amortization	6	35 326	11 420
Loans given	7	4 284 848	-4 284 848
Change in other receivables		-527 221	-69 771
Change in prepayments to suppliers		531 451	-541 686
Change in supplier payables		33 821	414 247
Change of accrued expenses and tax liabilities		186 235	-12 372
Increase of provision		700 000	1 680 000
Total change in working capital		**5 244 460**	**-2 803 010**
Total cash flow from / cash used in operating activities		**1 778 387**	**-12 345 977**
Cash flow from investing activities			
Purchase of property, plant and equipment	6	-50 472	-43 886
Purchase of short-term financial investments		-24 954 243	-8 029 395
Sales of short-term financial investments		14 012 248	13 261 332
Purchase of long-term financial investments	5	-9 387 960	0
Dividends and interest received		967 941	91 307
Total cash used in / cash flow from investing activities		**-19 412 486**	**5 279 357**
Cash flow from financing activities			
Paid in share capital	10	0	20 000 000
Total cash flow from financing activities		**0**	**20 000 000**
Total cash flow		**-17 634 099**	**12 933 380**
Cash and cash equivalents at beginning of the period	2	19 157 073	6 417 020
Change in cash and cash equivalents		**-17 634 099**	**12 933 380**
Effect of exchange rate differences[1]		-52 891	-193 327
Cash and cash equivalents at the end of the period	**2**	**1 470 083**	**19 157 073**

[1] The item includes the effect of exchange rate changes in bank accounts

Statement of changes in equity

(in Estonian kroons)

	Share capital	Share premium	Accumulated loss	Total equity
Balance as at 01.01.2006	**43 000 000**	**4 100 000**	**-9 158 143**	**37 941 857**
Share capital increase	20 000 000	0	0	20 000 000
Net loss for financial year	0	0	-6 153 784	-6 153 784
Balance as at 31.12.2006	**63 000 000**	**4 100 000**	**-15 311 927**	**51 788 073**
Balance as at 01.01.2007	**63 000 000**	**4 100 000**	**-15 311 927**	**51 788 073**
Net loss for financial year	0	0	-363 269	-363 269
Balance as at 31.12.2007	**63 000 000**	**4 100 000**	**-15 675 196**	**51 424 804**

More detailed information on share capital is provided in Note 10.

Notes to the Financial Statements

Note 1 Accounting policies and measurement bases adopted in the preparation of the financial statements

1.1 General principles

The financial statements of AS LHV Varahaldus have been prepared in accordance with the accounting principles generally accepted in Estonia, whose main requirements are prescribed by the Accounting Act of the Republic of Estonia and that are supplemented by the guidelines issued by the Accounting Standards Board. The financial statements have been prepared under the historical cost convention, except as disclosed in the accounting policies below.

The financial statements are presented in Estonian kroons.

1.2 Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise deposits held at call with banks as well as those in the investment account at AS Lõhmus, Haavel & Viisemann, as well as term deposits with original maturities of three months or less.

1.3 Shares and other securities

Securities held for the purpose of trading are classified as short-term shares and other securities. Other long-term shares and securities include securities not expected to be sold within the next 12 months.

Short and long-term investments in shares and other equity instruments are subsequently carried at fair value, if their fair value can be measured reliably. Shares and other equity instruments which fair value cannot be measured reliably are recognised at cost (that is acquisition cost less any impairment, when the carrying amount of the investment is not recoverable). The fair value of shares and other securities listed on the stock exchange is their quoted closing bid price. Fund units are measured at their redemption price. The purchases and sales of financial investments are recognised on the trade date. The changes in fair value of shares and other securities acquired for the purpose of trading are reported as gains or losses in the income statement of the accounting period. Gains or losses from changes in fair value of long-term financial investments are reported in the income statement of the accounting period.

All financial investments in this annual report are accounted at fair value.

1.4 Trade receivables

All receivables (accrued income, loans granted and other short and long-term receivables), except for receivables acquired for the purpose of selling, are carried at amortised cost. The amortised cost of the short-term receivables normally equals their cost value (less any impairment); therefore short-term receivables are stated in the balance sheet in their redemption value. Long-term receivables are initially recognised at the fair value of the consideration receivable and subsequently interest income is calculated on the receivable using the effective interest rate method. Receivables acquired for selling purposes are measured at fair value.

Impairement of trade receivables is accounted in case there is objective evidence that the estimated collections do not correspond to initial terms of contract. Such situations, that indicate on possible downturn of value of trade receivables, are the buyers' bankruptcy or significant financial difficulties and inability to fulfil their obligations. Impairement of trade receivables (i.e. the need for allowance) is assessed individually of each specific debtor, on basis of estimated present value of future cash flows. The value of impairment loss of trade receivables is the difference between the carrying value of these receivables and present value of future cash flows, using effective interest rate method. The carrying value of trade receivables is reduced by the amount of imapairment loss of receivables and loss from impairment is charged to the income statement as operating expenses. If the receivable is assesed to be irrecoverable, it is removed from the balance sheet. The collection of previously recognised impairment loss is reversed by adjusting the allowance account.

1.5 Derivative financial instruments

Derivative financial instruments (forward and swap contracts) are reported in the balance sheet at their fair value. Fair value is the market value of derivatives. Gains and losses on derivative financial instruments are reported as income or expense for the period.

1.6 Property, plant and equipment

Property, plant and equipment are assets used in the operations of the Company with a useful life of over one year and a cost of over 10 000 kroons. Property, plant and equipment is initially recognised at its cost which consists of the purchase price (incl. customs duties and other non-refundable taxes) and other expenditures directly related to the acquisition that are necessary for bringing the asset to its operating condition and location. Property, plant and equipment is carried in the balance sheet at its cost less any accumulated depreciation and any impairment losses. Where an asset's carrying amount is greater than its estimated recoverable amount (higher of an asset's net selling price and its value in use), it is written down immediately to its recoverable amount.

Subsequent expenditures on property, plant and equiptment are accounted as non-current assets when it is probable that the company will gain future economic benefit from these assets and the cost of the asset can be measured reliably. Other repair and maintenance costs are recognised as expenses at their occurrence.

Depreciation is calculated on the straight-line basis. The annual depreciation rate for software is 33%. Depreciation is commenced at the time when the asset can be used for the purpose intended by management and is terminated when the residual value exceeds the carrying amount, until the final removal of the asset from use or upon reclassification into "non-current assets held for sale". At each balance sheet date, the validity of depreciation rates, the depreciation method and the residual value is assessed.

The accounting of property, plant and equipment is terminated when asset is sold or when no more economic benefits can be gained from use or sale of the asset. The gain or loss from disposal of non-current asset is recognised in income statement as other operating revenues or other operating expenses.

1.7 Intangible assets

An intangible asset is initially recognised at cost, comprising of its purchase price and any directly attributable expenditure. After initial recognition, an intangible asset is carried in the balance sheet at its cost less any accumulated amortisation and any accumulated impairment losses.

Intangible assets with indefinite useful lives (goodwill which arose in a business combination) are not subject to amortisation, but an impairment test is carried out at each balance sheet date to review their value. The impairment test on intangible assets that are amortised is carried out when thre are indications, that the value of the assets may have impaired. If their recoverable amount turns out to be lower than their carrying amount, they are written down to their recoverable amount. The recoverable amount of the asset is the higher of the fair value less costs to sell or its value in use. For the purpose of assessing impairment, the recoverable amount is assessed either for each individual asset or the smallest group of assets for which it is possible to distinguish cash flow. The impairment loss of assets is reported as expenses in the accounting period.
The depreciation rate for intangible assets with definite useful lives is 33%.

1.8 Goodwill

Goodwill represents the excess of the acquisition cost over the fair value of the share of the net assets acquired, reflecting the part of acquisition cost which was paid for such assets of the acquired company which cannot be separated and accounted for separately. At the transaction date, goodwill is recognised in the balance sheet at its acquisition cost as an intangible asset. Goodwill is subsequently carried at its cost less any impairment losses. Goodwill is not amortised. Goodwill is not subject to amortisation, instead an impairment test is carried out at each balance sheet date (or more frequently when an event or change in circumstances indicates that the fair value of goodwill may have become impaired), an impairment test is performed and if necessary, goodwill is written down to its recoverable value if it is lower than its carrying amount.

1.9 Operating lease

Leases of property, plant and equipment where all significant risks and rewards of ownership are not transferred to the lessee are classified as operating lease. Payments made under operating leases are charged to the income statement on a straight-line basis over the lease term.

1.10 Financial liabilities

All financial liabilities (supplier payables, accrued expenses, and other short-term borrowings) are initially recorded at the acquisition cost, that includes all transaction costs related to acquisition. After initial recognition, financial liabilities are measured at amortised cost. To calculate the amortised cost of financial liabilities, they are initially recorded at fair value of the proceeds received (less transaction costs), taking into consideration the interest expence in following periods using effective interest rate method. Financial liabilities are classified as short-term, when their payment date is within 12 months after the balance sheet date or the Company does not have an unconditional right to postpone the settlement of the liability for later than 12 months after the balance sheet date.

1.11 Provisions and contingent liabilities

Commitments arising from an obligating event before the balance sheet date, which realisation time or amount are not certain, are recognised as provisions in the balance sheet. The provisions are recognised based on the management´s estimates regarding the amount and timing of the expected ouflows. A provision is recognised in the balance sheet in the amount which according to the management is necessary as at the balance sheet date for the meeting of the obligation arising from the provision or transfer to the third party. Other possible or existing contingent obligations, for which it is not probable that an outflow of resources will be required to settle the obligation; or the amount of the obligation cannot be measured with sufficient reliability, are disclosed in the notes to the financial statements as contingent liabilities.

1.12 Foreign currency transactions and assets and liabilities denominated in a foreign currency

Foreign currency transactions are recorded based on the foreign currency exchange rates of the Bank of Estonia prevailing at the dates of the transactions. Monetary financial assets and liabilities and non-monetary financial assets and liabilities - measured at fair value - denominated in foreign currencies as at the balance sheet date are translated into Estonian kroons based on the foreign currency exchange rates of the Bank of Estonia prevailing at the balance sheet date. Profits and losses from foreign currency transactions are recognised in the income statement as income or expenses of that period.

Non-monetary assets and liabilities nominated in foreign currency (prepayments, non-current assets) are not revaluated on balance sheet date, but accounted continuously at the Estonian Cenral Bank rate as of transaction date.

1.13 Revenues and expenses

Revenue and expenses have been recognised under the accrual basis of accounting. Revenue is recognised when the sold service has been provided and the risks and benefits have been transferred to the buyer and AS LHV Varahaldus has the right for the receivable. Revenue arising from interest and dividends is recognised when it is probable that the economic benefits associated with the transaction will flow to the enterprise and the amount of the revenue can be measured reliably. The management fees related to activities of investment funds are accounted during the period of providing services. Interest income is recognised taking into account the effective interest rate. Dividends are recognised when the right to receive payment is established.

1.14 Corporate income tax

According to income tax legislation currently in force the profit for financial year of a company is not a subject for taxation. Income tax is paid for dividends, fringe benefits, gifts, sponsorship, guest admission expenses, expenses not related to business and transfer pricing corrections. From 1.01.2008 the distribution of retained earnings is subject to a dividend tax of 21/79 (in 2007 the tax rate was 22/78 and in 2006 the tax rate was 23/77) of net dividend paid. In certain circumstances the dividends received can be distributed forward without additional income tax expense. The income tax law stipulates the income tax rate decrease until the year 2001: in 2009 the tax rate is 20/80, in 2010 the tax rate is 19/81 and from 2011 the tax rate is 18/82 of the net dividend paid. The corporate income tax related to dividend payments is accounted as liability and tax expence in income statement the same period the dividend is announced, no matter for which period the dividend is announced or when the divident payment is actually carried out. The liability for income tax payment is on the 10 day of the next month of dividend payment.

Arising from individuality of taxation there are no differences related to tax calculations and book values of assets and derived from that also not deferred tax receivables or liabilities. Contingent tax liabilities, that would arise from dividend payments from retained earnings, are not accounted in balance sheet. The maximum tax liability, that would accompany with profit distribution as dividends, is presented in notes for the financial reports.

1.15 Staturory reserve capital

Statutory reserve capital is formed to comply with the requirements of the Commercial Code. Statutory reserve capital is formed from annual net profit allocations. During each financial year, at least one-twentieth of the net profit shall be entered in reserve capital, until reserve capital reaches one-tenth of share capital. Statutory reserve capital may be used to cover a loss, or to increase share capital. Payments shall not be made to shareholders from statutory reserve capital.

Note 2 Cash and cash equivalents

	31.12.2007	31.12.2006
Bank account at Hansabank	1 451 380	19 156 703
Investment account at LHV	18 703	370
Total cash and cash equivalents	**1 470 083**	**19 157 073**

Note 3 Short-term financial investments

	31.12.2007	31.12.2006
Shares	207 006	0
Bonds	12 887 704	3 005 716
Fund units	2 175 710	0
Total at fair value through profit or loss	**15 270 420**	**3 005 716**

Note 4 Derivatives

	Receivable/liability (at fair value)	Contingent assets (contract amount)	Commitments (contract amount)
USD/EUR forward	254 152	7 799 920	7 545 768
EUR/USD forward	-197 000	7 602 920	7 799 920
Balance as at 31.12.2006	**57 152**	**15 402 840**	**15 345 688**

As at 31.12.2007 there were no forward contracts. The forward contracts in 2006 were entered into to hedge the foreign exchange risk derived from securities positions. The underlying assets of the purchase forward as at 31.12.2006 was 500 000 EUR. As all the securities denominated in USD were sold during the period of validity of the forward contract, the selling forward deal was concluded for 500 000 EUR to settle the position. Both contracts ended at 30.01.2007.

Note 5 Long-term financial investments

	31.12.2007	31.12.2006
Units of pension funds	29 041 685	27 669 992
Units of investment funds	8 938 464	0
Total at fair value through profit or loss	**37 980 149**	**27 669 992**

Units in investment funds have been purchased with their nominal value and the total purchase price of these fund units is 9 387 960 kroons.

Note 6 Property, plant and equipment and intangible assets

	Property, plant and equipment	Intangible assets	
	IT equipment	Licences	Goodwill
Balance as at 31.12.2005			
Acquisition cost	**21 500**	**0**	**1 183 699**
Accumulated depreciation	-4 730	0	0
Carrying value	**16 770**	**0**	**1 183 699**
Changes occurred in 2006			
Purchase of non-current assets	25 623	18 263	0
Depreciation / amortization charge	-9 914	-1507	0
Balance as at 31.12.2006			
Acquisition cost	**47 123**	**18 263**	**1 183 699**
Accumulated depreciation / amortization	-14 644	-1 507	0
Carrying value	**32 479**	**16 756**	**1 183 699**
Changes occurred in 2007			
Purchase of non-current assets	47 404	3 068	0
Depreciation / amortization charge	-28 379	-6 947	0
Balance as at 31.12.2007			
Acquisition cost	**94 527**	**21 331**	**1 183 699**
Accumulated depreciation / amortization	-43 023	-8 454	0
Carrying value	**51 504**	**12 877**	**1 183 699**

The balance sheet of AS LHV Varahaldus under the line intangible assets includes positive goodwill in the amount of 1 183 699 kroons which arose from the acquisition of former fund manager AS Seesam Varahaldus.

As at 31.12.2007 an impairment test was performed. Three former funds of Seesam Varahaldus have been designated as the cash-generating unit for goodwill testing. Calculation of the value in use is based on the following assumptions:

- in forecasting the cash flows for the years 2008-2012, the Management Board has assesed the estimated growth in salaries to be 8%, according to which the clients investments into funds have been derived
- the increase in volume of assets in funds exceeds the leaving clients from funds
- the growth rate used for indirect expenses is 10%
- cash flow discount rate used is 7%
- using key assumptions the management has relied on previous periods experiences and the best estimation of probable expectations.

According to the impairment test the recoverable value exceeds substantially carrying value of goodwill, therefore no impairment has been identified.

Note 7 Related party transactions

Related parties are owners, members of the Management Board and the Supervisory Board, companies related to them as well as funds managed by AS LHV Varahaldus.

The owners of AS LHV Varahaldus are:

AS LHV Group	61,96%
European Bank for Reconstruction and Development (EBRD)	19,04%
Seesam Elukindlustuse AS	19,00%

In 2007 the services from AS Lõhmus, Haavel & Viisemann (LHV, another subsidiary of the parent company) for rent and administration were bought for 1 779 548 kroons. The expenses have been accounted as part of operating expenses in income statement. As at 31.12.2007 the liability to LHV is 86 937 kroons. In 2006 the services were bought for 740 443 kroons and sold for 7 133 kroons. As at 31.12.2006 there are loans granted backed by securities presented in balance sheet in amount of 4 284 848 kroons, that are granted to LHV with due date in March, 2007 and collected in time. There were no liabilites to related parties as at 31.12.2006.

Management fees	**Revenues 2007**	**Receivable as at 31.12.2007**	**Revenues 2006**	**Rreceivable as at 31.12.2006**
Pension funds	7 386 213	728 873	4 785 329	495 760
Investment funds	350 375	76 383	0	0
	7 736 588	**805 256**	**4 785 329**	**495 760**

During the accounting period salaries were paid to management board members in amount of 522 045 kroons (2006: 344 784 kroons). No remunerations were made to supervisory board members.

The company has not yet signed the management service contracts with management board members by the time of signing this report. The employment contracts have been entered into with the management board members and therefore they are entitled to compensation in case of dispense from duties according to Estonian employment contract act.

There were no impairment losses recognised in receivables of related parties in 2007 or 2006.

Note 8 Accrued expenses and other liabilities

	31.12.2007	**31.12.2006**
Payables to employees	222 753	108 971
Tax liabilities	219 569	147 116
incl. social security tax	120 103	81 710
incl. personal income tax withheld	78 296	60 332
incl. unemployment insurance premium	2 840	2 181
incl. contributions to mandatory pension	6 166	4 127
incl. corporate income tax	10 870	-1 234
incl. value added tax	849	0
incl. tax penalties	445	0
Total	**442 322**	**256 087**

Note 9 Provisions

AS LHV Varahaldus has given DVD-players and gift-cards to clients joining the pension funds in previous periods, which are handled as expenses related to business. As the discussion with tax authorities is still in progress on the date of compiling this financial statement, whether to recognise these items as purely advertising costs or gifts, there is formed a provision for possible corporate income tax and interest liabilities in the amount 1 300 000 kroons in 2004, 1 200 000 kroons in 2005, 1 680 000 kroons in 2006 and 700 000 kroons in 2007. As the management board can not assess the time of final conclusions of the discussion, the provision has been set as short-term liability.

Note 10 Share capital

At the end of 2006 the company´s share capital increase was carried out with issue of new shares. 2 000 000 new shares at par value of 10 koons were issued. In total 20 000 000 kroons was paid in cash. As at 31.12.2007 the company´s share capital is 63 000 000 kroons, which consits of 6 300 000 shares with nominal value of 10 kroons.

Note 11 Fee income

Activity – fund management	**2007**	**2006**
Pension fund management (note 7)	7 386 213	4 785 329
Investment fund management (note 7)	350 375	0
Fund issue and redemtion fees	1 969 198	1 207 507
Total	**9 705 786**	**5 992 386**

In the financial year and in 2006, the Company's services were rendered only in Estonia.

Note 12 Operating expenses

	2007	**2006**
Marketing expenses	4 078 689	7 344 835
Advertising costs	1 202 464	1 767 364
Other outsourced services	1 500 245	1 146 475
Depository fees	787 254	480 782
Registration fees	430 077	406 495
Supervision and guarantee fees	284 592	318 528
Legal consultations and audit	265 572	292 037
Office expenses	494 590	144 686
Communication costs	199 438	64 722
Travel and training expenses	166 989	65 053
Transport expenses	82 693	350 328
Bank services, management and transaction fees	55 695	78 694
IT expenses	24 146	12 036
Total operating expenses	**9 572 444**	**12 472 035**

Note 13 Operating lease

The Company leases office space and a passenger car under the operating lease terms. In the financial year, the rent for the office space totalled 445 804 kroons and lease payments for the passenger car totalled 66 105 kroons. In 2006, the rent for office space was 110 874 kroons and the car lease payments were 161 808 kroons. Operating lease expenses are accounted as a part of operating expenses in income statement.

Note 14 Contingent liabilities

Tax authorities have the right to review to the Company's tax records for up to 6 years after submitting the tax declaration and upon finding errors, impose additional taxes, interest and fines. The Company's management estimates that there are not any circumstances which may lead tax authorities to impose additional taxes on the Company.

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INDEPENDENT AUDITOR'S REPORT

(Translation of the Estonian original)*

To the Shareholders of AS LHV Varahaldus

We have audited the accompanying financial statements of AS LHV Varahaldus (the Company) which comprise the balance sheet as of 31 December 2007 and the income statement, statement of changes in equity and cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory notes.

Management Board's Responsibility for the Financial Statements

Management Board is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in Estonia. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the accompanying financial statements give a true and fair view of the financial position of the Company as of 31 December 2007, and of its financial performance and its cash flows for the year then ended in accordance with accounting principles generally accepted in Estonia.

Urmas Kaarlep
AS PricewaterhouseCoopers

Relika Mell
Authorised Auditor

7 April 2008

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* *This version of our report is a translation from the original, which was prepared in Estonian. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation.*

Proposal for allocation of net loss for financial year

The Management Board of AS LHV Varahaldus proposes to the General Meeting of Shareholders to add the loss for 2007 in the amount of 363 269 kroons to the accumulated losses from previous years.

Signatures of the Management Board and the Supervisory Board to the 2007 Annual Report

The Management Board has prepared the management report and the financial statements of AS LHV Varahaldus for the financial year ended on 31 December 2007.

The Suprevisory Board has reviewed the annual report, which consits of management report and financial statements, independent auditor´s report and the proposal of allocation of net loss for financial year and approved it for presentation at the General Meeting of Shareholders.

MANAGEMENT BOARD
07.04.2008

Members of the Management Board:

Mihkel Oja ....

Rain Lõhmus ....

Rait Kondor ....

SUPERVISORY BOARD
08.04.2008

Chairman of the Supervisory Board

Andres Viisemann ....

Members of the Supervisory Board:

Liisi Ruus ....

Erki Kilu ....

Charles Smith ....