

AS VENTSPILS NAFTA

(UNIFIED REGISTRATION NUMBER 50003003091)

**CONDENSED ANNUAL REPORT
FOR THE YEAR ENDED 31 DECEMBER 2005**

PREPARED IN ACCORDANCE WITH THE LAW OF THE REPUBLIC OF LATVIA
ON FINANCIAL STATEMENTS OF COMPANIES

Ventspils, 2006

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General information

Name of the company	AS Ventspils nafta
Legal status of the company	Joint stock company
Unified registration number, place and date of registration	50003003091 Riga, 9 May 1991 Registered with the Commercial Register on 5 August 2004
Registered office	Talsu iela 75, LV-3600, Ventspils, Republic of Latvia
Subsidiaries	SIA LatRosTrans (66%) Balvu iela 7, LV-5043, Daugavpils SIA Ventspils nafta termināls (100%) Talsu iela 75, LV-3600, Ventspils AS Preses nams (92.92%) Balasta dambis 3, LV-1081, Riga SIA Mediju nams (90.21%) Balasta dambis 3, LV-1081, Riga SIA Rīgas Iīcis VN (100%) Dubultu prospekts 51, LV-2015, Jūrmala SIA Nekustamie īpašumi VN (100%) Balasta dambis 3, LV-1081, Riga
Associated entities	AS Latvijas kuģniecība (49.94%) Basteja bulvāris 2, LV-1807, Riga SIA Mediji un Poligrāfija (32.70%) Balasta dambis 3, LV-1081, Riga SIA Ventshoes (21.44%) I.Mičurina iela 6, LV-3601, Ventspils SIA Futbola klubs Ventspils (30%) Dzintaru iela 20a, LV-3602, Ventspils

General information (cont'd)

Subsidiaries of SIA Nekustamie
īpašumi VN

SIA Darījumu centrs Daugava (100%)
Balasta dambis 3, LV-1081, Rīga

SIA Namserviss VN (100%)
Balasta dambis 3, LV-1081, Rīga

SIA Ventspils biznesa centrs (100%)
Balasta dambis 3, LV-1081, Rīga

SIA Maikapara nams under liquidation (100%)
Balasta dambis 3, LV-1081, Rīga

SIA Lejastiezumi (100%)
Balasta dambis 3, LV-1081, Rīga

SIA Pārventas sporta centrs (100%)
Balasta dambis 3, LV-1081, Rīga

Financial year

1 January – 31 December 2005

Management report

The year 2005 was marked for joint stock company AS Ventspils nafta both with improvement of the Group's financial figures and growth of the AS Ventspils nafta share price on Riga Stock Exchange, thus clearly demonstrating the overall growth of AS Ventspils nafta Group's value.

The key objectives of AS Ventspils nafta, as the holding company of the Group, set for the reporting period are to add Group's value, which comprises successful development of the all the branches of the Group, achieving the increase in value for each particular entity. To attain this objective, the holding company manages AS Ventspils nafta investment activity on the business line level, including strategic planning for the Group companies, organisation and monitoring of operational planning, as well as financial, investment, and tax management and planning for the Group, internal audit for the Group companies, preparation of consolidated financial statements, and identification, analysis and management of new investment projects.

In the reporting period the registered and paid-up share capital of AS Ventspils nafta was LVL 104 479 519 and consisted of 104 479 519 shares. The par value of each share was LVL 1. 60 598 121 shares are listed on Riga Stock Exchange (i.e. publicly traded).

In 2005 the price of AS Ventspils nafta shares on Riga Stock Exchange ranged from LVL 1,70 to LVL 2,73; the average share price reached LVL 2,07, which is by 57 santims more than in 2004, when the average price of AS Ventspils nafta shares constituted LVL 1,50. The total of 1 068 000 shares was traded during 2005 on Riga Stock Exchange, thus reaching the annual turnover of LVL 2 213 000. The market capitalisation of AS Ventspils nafta shares as at the end of 2005 was LVL 282,1 million, with the average market capitalisation having increased from LVL 156,4 million in 2004 to LVL 216,5 million in 2005, which is more by LVL 60,1 million or 38,4% in accordance with the share price growth.

Such results of AS Ventspils nafta share quotation in 2005 clearly show the impact of the improved performance of AS Ventspils nafta Group in the reporting period. Pursuant to the financial statements of AS Ventspils nafta for the year ended 31 December 2005 prepared in accordance with the Law of the Republic of Latvia on Financial Statements of Companies, the net loss of AS Ventspils nafta has reached LVL 35 million, which is due to the changes in the accounting policies in respect to disclosures of changes in the value of subsidiaries and associated entities in the parent company's statements.

For comparability and consistency purposes, certain items of the prior year income statement and balance sheet were adjusted considering changes in the accounting policies made in 2005. Such adjustment of prior financial statements is contemplated by Latvian and International Financial Reporting Standards. The adjusted financial statements for the year ended 31 December 2004 will be presented together with the audited financial statements for the year ended 31 December 2005.

In view of the requirements of International Financial Reporting Standards, AS Ventspils nafta has recorded in its financial statements for the year ended 31 December 2005 non-recurrent expense related to partial impairment of technological assets of subsidiaries SIA LatRosTrans and SIA Ventspils nafta termināls due to the three years long idleness of the oil pipeline. Considering the aforementioned impairment, the negative financial result of LVL 35 million from investments in subsidiaries and associated entities is recorded in the financial statements of AS Ventspils nafta for the year ended 31 December 2005. Since this expense is non-recurrent, future financial results of AS Ventspils nafta will not be affected thereby.

Regardless of the advantages and high quality of the Ventspils oil transit corridor admitted by Russian oil exporters, oil transportation via the pipeline to Ventspils port was ceased in January 2003 in the result of the economically unreasonable decision taken by Russian state authorities without consulting other parties. Since 2003 the auditors of AS Ventspils nafta have been repeatedly stressing in their reports the potential necessity to record impairment of the assets of the Group companies engaged in oil piping due to ceased oil transportation to ensure compliance with the requirements of International Financial Reporting Standards.

Since oil has not been transported via the pipeline for three years already, the auditors of AS Ventspils nafta indicate that this period is sufficient for the impairment recognition to be mandatory. After the oil pipeline in the Ventspils direction had been closed, AS Ventspils nafta Council and Board were actively working both at the local and international level to ensure equal possibilities for Russian oil export and renewal of oil transit via the pipeline to Ventspils. However, observing the political status of the Russian authorities which took this decision, solution of the problem was not possible due to limited influence of AS Ventspils nafta. At the same time, the management of AS Ventspils nafta believes that oil transportation via the pipeline in the Ventspils direction would be the most optimal and advantageous route for Russian oil export to North Western Europe and is still confident that oil transportation in this direction may be renewed.

During the reporting period SIA Ventspils nafta termināls, a subsidiary of AS Ventspils nafta, displayed its ability to quickly adapt to the actual situation and market conditions. Regardless of the ceased crude oil transit via the pipeline, SIA Ventspils nafta termināls managed to substantially increase the amount of reloaded oil products received by railway, i.e. petrol of various grades and diesel fuel with different sulphur content. Compared to the year 2004, the amount of petrol and diesel fuel reloaded by the terminal has increased by 1,2 million tons and 0,3 million tons respectively.

Management report (cont'd)

The reloading volumes of SIA Ventspils nafta termināls have increased owing to the active work for attraction of customers, and introduction of new and beneficial kinds of services, including petrol loading into tankers having the deadweight of up to 100 000 tons. No competitor of SIA Ventspils nafta termināls currently supplies this kind of service. The same refers also to standing oil storage in tanks. In the reloading structure of SIA Ventspils nafta termināls, the decrease by 1,8 million tons compared to the previous year may be observed only with regard to crude oil transported by railway.

Being affected by high oil prices prevailing on the world markets, Russia substantially increased import tax on oil in 2005. As a result, oil export by railway became unprofitable, and the export volumes diminished almost in all Russian oil transit routes.

In 2006 SIA Ventspils nafta termināls aims at increasing the amount of reloaded oil and oil products received by railway, meanwhile retaining its market share in reloading of oil and oil products exported from Russia and other CIS countries by railway. SIA Ventspils nafta termināls plans to continue cooperation with existing business partners and attract new clients by offering a competitive tariff policy, a beneficial assortment of services and high-quality servicing. In competition with other companies, the technological advantages of SIA Ventspils nafta termināls enable it to extend the assortment of reloaded products depending on the specific market conditions, as well as to offer tank lease and oil storage services. In 2006, under the company's investment programme, SIA Ventspils nafta termināls plans to commence the first stage of new pipeline corridor construction to join together the terminal and piers.

During the reporting period SIA LatRosTrans, a subsidiary of AS Ventspils nafta owning and operating oil and oil products pipelines, recorded 20,3 million tons of transported oil and oil products, which is by 0,8 million tons more than in 2004. Continuing implementation of the development program, SIA LatRosTrans invested more than LVL 8 million in the construction of the main pumping station, modernisation of the communication system and other technical upgrading projects. The purposeful work done by the management of SIA LatRosTrans in 2005 resulted in a significant decrease of excess physical losses of oil products caused by unauthorised actions.

In the result of technological solutions implemented in the reporting period, the capacity of the oil products pipeline belonging to SIA LatRosTrans has already reached 8 million tons per annum, and this will permit SIA LatRosTrans to increase diesel fuel transportation volumes and improve its profitability in the upcoming year. In 2006 SIA LatRosTrans plans to increase the total amount of transported oil and oil products and use the pipeline capacity to the maximum extent possible, ensuring transportation of diesel fuel to Ventspils and oil transportation to Mažeikiai oil refinery and Butinge oil terminal. Within the framework of the investment program, in 2006 SIA LatRosTrans intends to make investments in construction of the oil product accounting point in Skrudaliena and modernisation of the communication system. In addition, SIA LatRosTrans will continue the active work for reduction and, if possible, prevention of excess physical losses of diesel fuel above the limits set by Latvian laws.

The reporting period was crucial for another subsidiary of AS Ventspils nafta - the largest Baltic printing group AS Preses nams. The company continued successful optimisation of its organisational and functional structure which was commenced in 2004. In 2005 the construction of two new and modern production facilities of AS Preses nams was commenced. One of the facilities is intended for printing of newspapers and magazines, and the other for book printing. In the reporting period AS Preses nams managed to retain its leading position in the Baltic printing market. The net turnover of the company has reached LVL 21,5 million, which is by LVL 2,3 million more than in 2004. The increase in the sales in 2005 constitutes 13% compared to 2004. The proportion of intra-Community exports by AS Preses nams is 30%. The amount of investments made by AS Preses nams in modernisation and development projects in 2005 reached LVL 14,3 million.

The strategic goals of AS Preses nams set for 2006 comprise maintaining and strengthening of its position in the printing market and increase of the company's value, by expanding its market share and ensuring sales growth, optimising the management and production structure, as well as continuing upgrading of production equipment. AS Preses nams plans to commence production in the new printing facilities in the second half of 2006.

The year 2005 was a period of positive changes for AS Latvijas kuģniecība, an associated entity to AS Ventspils nafta. Ensuring equality of shareholders' rights and transparency of the management functions, the new Council and Board of AS Latvijas kuģniecība started working in 2005. While strengthening its competitiveness, AS Latvijas kuģniecība continued implementation of the tanker upgrading programme. Within the framework of this programme, 14 new tankers were ordered from Croatian and Korean shipyards. The first tanker is to be launched into operation in the middle of 2006.

Business risk diversification policy pursued by AS Ventspils nafta over past few years has resulted in a number of liquid financial investments in real estates, several of which are located in the centre of Riga and Jūrmala. The market value of these estates has already substantially exceeded initial investments. According to International Financial Reporting Standards and changes of Latvian laws whereby part of real estates may be reclassified as investment properties since 2005, and therefore estates may be recorded at their fair value not acquisition cost, AS Ventspils nafta restated as investment properties three estates: the land plot at Balasta dambis 3 on which the building of AS Preses nams is located, the land plot and building in Old Riga, Palasta iela 10, the land plot and buildings in Jūrmala, Dubultu prospekts 51.

Management report (cont'd)

In the reporting period favourable changes were observed in the operations of one more subsidiary of AS Ventspils nafta - SIA Mediju nams, one of the leading Latvian publishing houses. In 2005 SIA Mediju nams issued three newspapers and four magazines addressing different reader categories; its net turnover has reached LVL 2,9 million, which is by LVL 0,2 more than in 2004. Regardless of the tough competition in all segments of Latvian printed media market, SIA Mediju nams succeeded in diminishing the expected loss from LVL 1,2 million in 2004 to LVL 0,9 million in 2005. The increase in revenues, optimisation of production processes and introduction of new products account for this success.

The year 2006 marked the 45th anniversary of the Ventspils port terminal where oil and oil products reloading operations were commenced in September 1961. Over the last years, the company has turned from a transit enterprise into a world famous group operating and scoring success in different business areas, and it is known today as AS Ventspils nafta. The year 2006 will be also important for further development of AS Ventspils nafta Group, as 38,6% of AS Ventspils nafta stock held by the state are to be sold according to government's decision, thus causing changes in the current shareholding structure. In 2006, in the same manner as previously, the management of the central holding company of AS Ventspils nafta Group will continue working to add the Group's value, facilitating successful development of and creation of added value for each business structure separately and the whole Group.

19 May 2006

On behalf of the Council:

On behalf of the Board:

Mamerts Vaivads
Chairman of the Council

Olga Pētersone
Chairperson of the Board

Income Statement

	2005	2004	2004
	LVL thousand	restated LVL thousand	reported LVL thousand
Net sales	3 981	1 359	1 359
Cost of sales	(2 626)	(1 359)	(1 359)
Gross profit	1 355	-	-
General and administrative expense	(2 218)	(1 639)	(1 639)
Other operating income	528	7 700	7 700
Other operating expense	(319)	(2 706)	(2 706)
Result from operating activities	(654)	3 355	3 355
Gain/ loss in subsidiaries and associated entities, net	-	-	9 955
Impairment of investments	(35 064)	(1 074)	-
Financial income/ (expense), net	446	(31)	(31)
Result before taxes	(35 272)	2 250	13 279
Corporate income tax	(6)	1 626	1 626
Other taxes	(80)	(127)	(127)
Net result for the year	(35 358)	3 749	14 778

On behalf of the Council:

On behalf of the Board:

Mamerts Vaivads
 Chairman of the Council

Olga Pētersone
 Chairperson of the Board

Balance Sheet
ASSETS

	31/12/2005	31/12/2004	31/12/2004
	LVL thousand	restated LVL thousand	reported LVL thousand
NON-CURRENT ASSETS			
Property, plant and equipment			
Land and buildings	5 007	5 123	-
Machinery and equipment	49	89	89
Other property, plant and equipment	431	589	589
Construction in progress	160	160	160
Prepayments for property, plant and equipment	72	-	-
TOTAL	5 719	5 961	838
Investment properties	621	628	5 751
Investments			
Investments in subsidiaries and associated entities	182 946	217 143	277 304
Long-term loan to related party	1 201	4 541	4 541
TOTAL	184 147	221 684	281 845
TOTAL NON-CURRENT ASSETS	190 487	228 273	288 434
CURRENT ASSETS			
Inventories	3 044	4 352	4 352
Accounts receivable			
Short-term loans to related parties	2 811	271	271
Accounts receivable from related parties	26	854	854
Corporate income tax receivable	265	17	17
Other accounts receivable	61	51	51
Prepaid expense	35	58	58
Securities	51	58	58
Cash and cash equivalents	1 697	79	79
TOTAL CURRENT ASSETS	7 990	5 740	5 740
TOTAL ASSETS	198 477	234 013	294 174

On behalf of the Council:

On behalf of the Board:

 Mamerts Vaivads
 Chairman of the Council

 Olga Pētersone
 Chairperson of the Board

Balance Sheet

LIABILITIES AND SHAREHOLDERS' EQUITY

	31/12/2005	31/12/2004	31/12/2004
	LVL thousand	restated LVL thousand	reported LVL thousand
SHAREHOLDERS' EQUITY			
Share capital	104 479	104 479	104 479
Share premium	42 343	42 343	42 343
Long-term assets revaluation reserve	-	-	48 918
Foreign currency translation reserve	-	-	(9 077)
Restricted reserves	-	-	17 224
Other reserves	86 394	82 645	74 712
Current year unappropriated result	(35 358)	3 749	14 778
TOTAL SHAREHOLDERS' EQUITY	197 858	233 216	293 377
LIABILITIES			
Long-term liabilities			
Finance lease liabilities	-	20	20
Deferred corporate income tax	321	315	315
TOTAL	321	335	335
Current liabilities			
Finance lease liabilities	22	-	-
Trade accounts payable	37	91	91
Accounts payable to related party	9	105	105
Taxes payable	20	95	95
Other liabilities	31	33	33
Accrued liabilities	179	138	138
TOTAL	298	462	462
TOTAL LIABILITIES	619	797	797
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	198 477	234 013	294 174

On behalf of the Council:

On behalf of the Board:

 Mamerts Vaivads
 Chairman of the Council

 Olga Pētersone
 Chairperson of the Board

Statement of Cash Flows

	2005	2004	2004
	LVL thousand	(restated) LVL thousand	(reported) LVL thousand
Cash flow from/ (to) operating activities			
Result before taxes	(35 272)	2 250	13 279
Adjustments			
(Gain)/ loss in subsidiaries and associated entities, net	-	1 074	(9 955)
Write-offs of investment value	35 064	-	-
Write-offs of securities	8	-	-
Amortisation and depreciaton	327	1 906	1 906
Interest income	(156)	(97)	(97)
Interest expense	6	10	10
(Loss)/ gain on disposals of tangible assets	3	(1 240)	(1 240)
Gain from revaluation of oil and oil products	-	(2 201)	(2 201)
Other adjustments	-	24	24
Operating profit/ (loss) before working capital changes	(20)	1 726	1 726
Decrease in inventories	1 308	369	369
Decrease/ (increase) in other accounts receivable	1 674	(640)	(640)
Increase/ (decrease) in current liabilities	(184)	(660)	(660)
Net cash from/ (to) operating activities	2 778	795	795
Taxes paid	(360)	(419)	(419)
Net cash from/ (to) operating activities	2 418	376	376
Cash flow from/ (to) investment activities			
Purchase of non-current assets	(83)	(78)	(78)
Proceeds from sale of tangible assets	-	10	10
(Increase) in investments	(867)	(886)	(886)
Interest received	156	97	97
Net cash flow from/ (to) investment activities	(794)	(857)	(857)
Cash flow from/ (to) financing activities			
Increase in own shares	-	90	90
Borrowings received	-	20	20
Interest payments	(6)	(10)	(10)
Net cash flow from/ (to) financing activities	(6)	100	100
Net increase/ (decrease) in cash	1 618	(381)	(381)
Cash at the beginning of the year	79	460	460
Cash at the end of the year	1 697	79	79

Statement of Changes in Shareholders' Equity

	Share capital	Share premium	Long-term assets revaluation reserve	Restricted reserves	Other reserves	Current year unappropriated result	Total
Balance as at 31 December 2003	104 479	42 343	712	11 210	84 617	(9 270)	234 091
Impact of change in accounting policy	-	-	(712)	-	(11 349)	7 437	(4 624)
Adjustment of reserves due to change in accounting policy	-	-	-	(11 210)	11 210	-	-
Balance as at 31 December 2003, restated	104 479	42 343	-	-	84 478	(1 833)	229 467
Transfer of 2003 net result	-	-	-	-	(1 833)	1 833	-
Current year result, restated	-	-	-	-	-	3 749	3 749
Balance as at 31 December 2004, restated	104 479	42 343	-	-	82 645	3 749	233 216
Transfer of 2004 net result	-	-	-	-	3 749	(3 749)	-
Current year result	-	-	-	-	-	(35 358)	(35 358)
Balance as at 31 December 2005	104 479	42 343	-	-	86 394	(35 358)	197 858