



J O I N T S T O C K C O M P A N Y

L A T V I J A S V A L S T S M E Ž I

A N N U A L R E P O R T

2005



LATVIJAS VALSTS MEŽI

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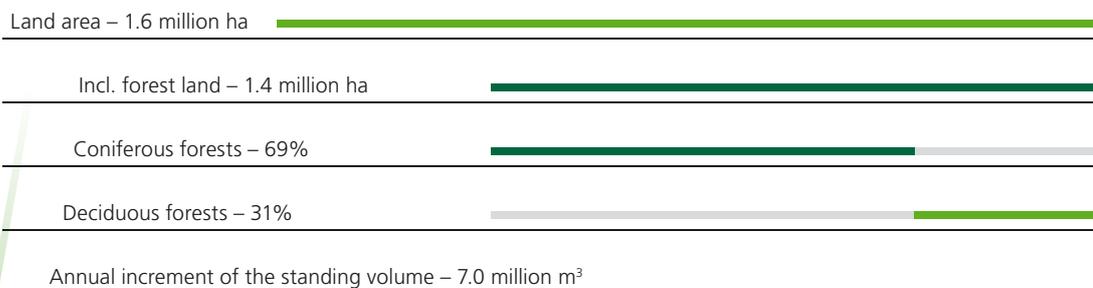
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Forests



Economic activities

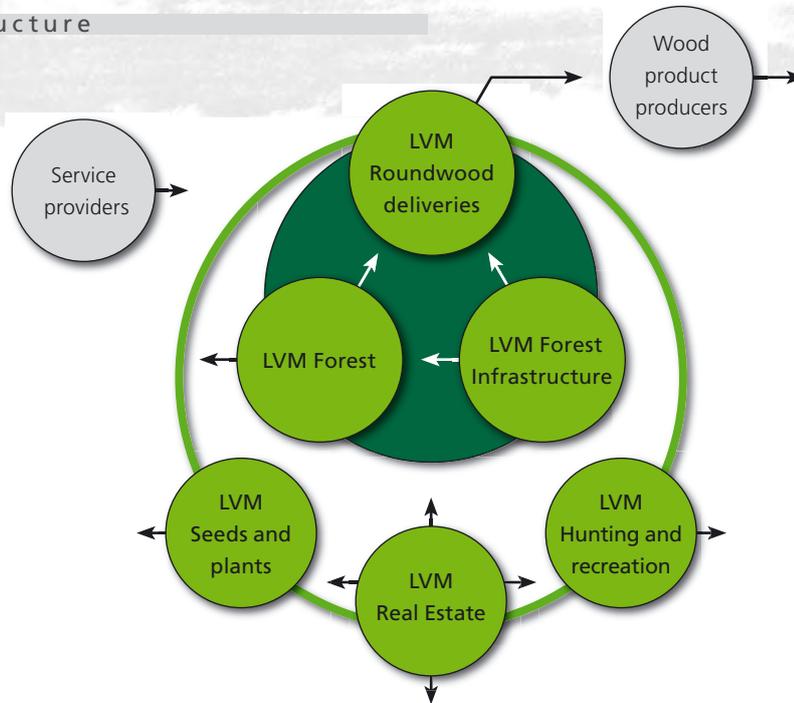
		2000.	2001.	2002.	2003.	2004.	2005.
Annual timber sales	million m ³	3.72	3.80	3.82	4.18	3.86	3.38
Incl. roundwood assortments	million m ³	–	–	0.01	0.34	0.73	1.40
Area of replanted forest	thousand ha	12.9	8.4	9.4	10.8	10.9	11.2
New stands tended	thousand ha	25.2	23.0	22.5	27.0	29.4	30.1
Forest roads built	km	–	191	340	383	520	617
Net sales	million LVL	16.8	22.2	27.7	45.9	65.2	69.5
Profit after taxes	million LVL	0.3	1.0	5.2	13.7	33.8	22.9
Investments	million LVL	2.3	0.7	4.9	6.5	11.4	17.1
Contribution to state and municipal budgets	million LVL	10.8	12.1	12.7	15.9	20.1	27.3

BRIEF FACTS

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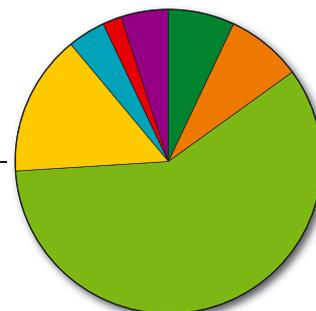
LVM structure



Number of employees

Administration	52	7%
LVM Roundwood deliveries	55	8%
LVM Forest	426	59%
LVM Seeds and Plants	109	15%
LVM Hunting and Recreation	27	4%
LVM Real Estate	18	2%
LVM Forest infrastructure	39	5%

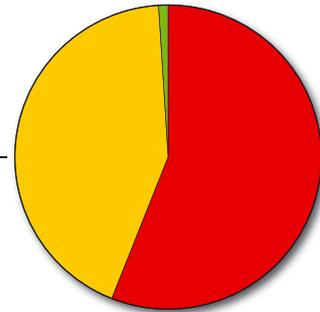
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Education

University	407		56%
Secondary	312		43%
Basic	7		1%

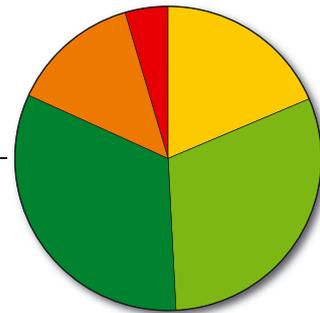
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Age

To age 30	135		19%
From 31 – 40	222		30%
From 41 – 50	237		33%
From 51 – 60	99		14%
Over 61	33		4%

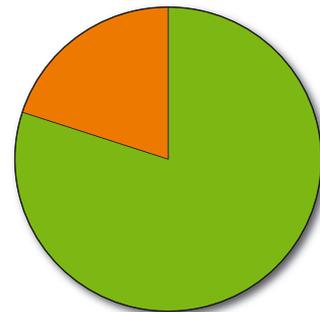
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Gender

Male	506		70%
Female	220		30%

726*



* excl. seasonally employed

BRIEF FACTS

BRIEF FACTS

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Roberts Strīpnieks,

Chairman of the Board of the joint stock company Latvijas valsts meži (Latvia's State Forests - LVM)

Last year was both one of the most difficult and most successful years in the history of the company. It was the most difficult because of a devastating storm on January 8 and 9, of a strength unseen for 40 years. It was successful because despite these difficulties, we fulfilled our ambitious development plans.

During the storm crisis, the company showed great flexibility and efficient decision-making at all levels of management. Large companies are generally assumed to be like super-tankers, which need several kilometers to turn around. The way how LVM approached storm clean up operations showed that we could work efficiently and react quickly in times of drastic change.

Thanks to all of the company employees! None of you were confused about how to handle the crisis in any of Latvia's districts. Within the first days after the storm, fallen trees were immediately removed from forest roads across the country and the normal functioning of forest infrastructure was restored. All of us were working even before the storm had abated.

We also must thank our timber buyers and service providers, none of whom

had any previous experience in dealing with such a nationwide natural disaster. This storm also showed that, when it comes to the battle against the forces of nature, the availability of a flexible logging and roundwood delivery system is the only support that forest owners have.

However, the storm didn't stop productive work at Latvia's State Forests (LVM). LVM started executing many new projects that were not connected to cleaning up after the storm. The subunit "LVM Hunting and Recreation" has changed its business model from a simple organization serving the needs of hunters to a niche-oriented tourist agency with great future potential. Thanks to the efforts taken last year, two new tourism and information centers at Ezernieki and Spare will start work in 2006. This will be a new, significant advance for eco-tourism in Latvia.



MANAGEMENT

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One should also mention the development plans of "LVM Seeds and Plants", which started last year and whose results we will see already this year. We can finally speak of a new, competitive export product. The first spruce plants have already been delivered to our customers in Sweden. Five years ago, no one would have believed that was possible.

Two new subunits were created in 2005 – "LVM Forest Infrastructure" and "LVM Real Property". The mission of the first is to ensure the construction of forest infrastructure such as roads, drainage systems, etc. By increasing the density of forest roads, the efficiency of forest management increases throughout the whole management cycle. Increased road access allows cuts in the costs of replanting and cultivation and reduces the distance wood must be hauled from felling to the nearest road, thereby increasing the value of the felling.

The subunit "LVM Real Property's" main task is to ensure the legal and rational management of real property managed or owned by LVM (land, buildings, structures, utility connections, etc.) and to ensure that these are available for meeting operational goals. A large number of staff was used in creating the subunit and a great amount of preparatory work was done to ensure that it could begin in 2006. All this took place at the same time as the storm cleanup.

We at LVM were highly honored to host the 6th Conference of the European State Forest Organizations, which took place on June 7–10, 2005 in Jūrmala, Latvia. This important event attracted CEO's and senior personnel from state forest management organizations in more than 20 countries. The representatives discussed common issues, exchanged experiences and focused on strengthening the network of the European state forest organizations. During the conference Latvia, along with Austria, Finland and France had the honour of participating in the foundation of an umbrella organization for the state forest managers – European State Forests Association (EUSTAFOR).

In the fall, a survey was conducted on the company's corporate culture. It determined the words and phrases that are most often used by our employees to describe the dominant values at LVM. Any owner or company leader would be proud of a staff which defines as its main values honesty, achievement, competence, cooperation, joy of living and pride in one's organization. After joining the European Union, rapid changes took place in Latvia. If we do not want to lose the greatest value of our company – educated and thinking people – we must find ways to work more effectively and productively. To mobilize these resources, we need everyone's help and advice.

Anatolijs Gorbunovs,
Chairman of the Supervisory Board, AS "Latvijas valsts meži"

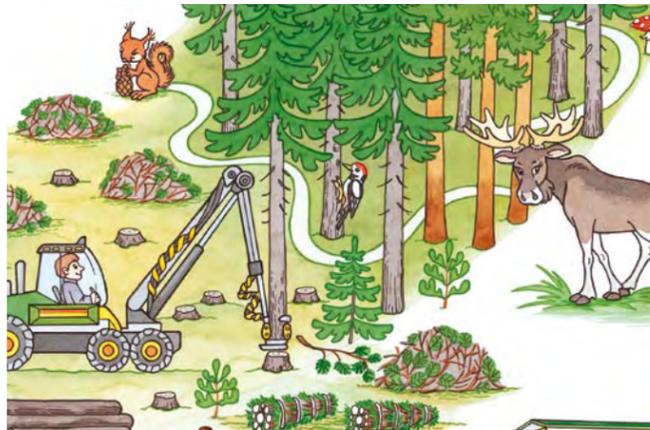
The Supervisory Board of AS "Latvijas valsts meži" (LVM), in examining the 2005 annual report and, in preparing a report to the shareholders, has determined that the LVM budget and operational plans for 2005 have been fulfilled.

The year 2005 stood out from the very start because a very powerful cyclone raged in Latvia on January 8–9, doing enormous damage to the forests. The forest areas administered by LVM suffered damage to around 3 million cubic meters of wood in the form of windfalls and trees broken by wind. As a result, the main task of LVM in 2005 was to rapidly clean up the extensive storm damage.

Another aspect that sharply illustrated the events of last year was the up to threefold fall in the price of coniferous standing timber caused by the rapid inflow of wind-felled wood from the state, private and neighbor-country forests. In addition, because the storm damaged extensive forest areas, the demand for forest harvesting and timber transport services increased significantly both in Latvia and other countries affected by the storm, resulting in an increase in the cost of these services of around 30 %. All these factors affected the financial results of LVM in 2005; therefore the shareholder amended the 2005 budget, reducing both net turnover and profit targets.

Even though the Cabinet of Ministers decided, after the cyclone, to add the storm damaged timber to the 2005 forest cutting plan, LVM, in drafting its operational strategy for 2005 after the storm, decided to only minimally increase the total cutting volume and basically focus on the harvesting of storm-damaged timber. As a result, some 2 million m³ of timber in state forestlands were left uncut, harvesting the storm-damaged timber instead. The uncut stands will continue to grow and provide high quality wood for the forestry branch and higher profits for LVM in coming years. Parallel to the harvesting of storm-damaged timber, LVM organized the reforestation of cuttings, which is very important in terms of the long-term management of state forest areas.

I wish to express my satisfaction that LVM has hitherto organized its works so that the company's various units were prepared to rapidly clean up the damage from the storm by as quickly as possible gathering damaged timber so that it suffered no loss of quality and could be sold advantageously for the state even under unfavorable market conditions. The fact that the company could successfully work under severe crisis conditions, not only on an everyday basis, confirms that LVM has hitherto correctly planned its work.



FOREST MANAGEMENT CYCLE

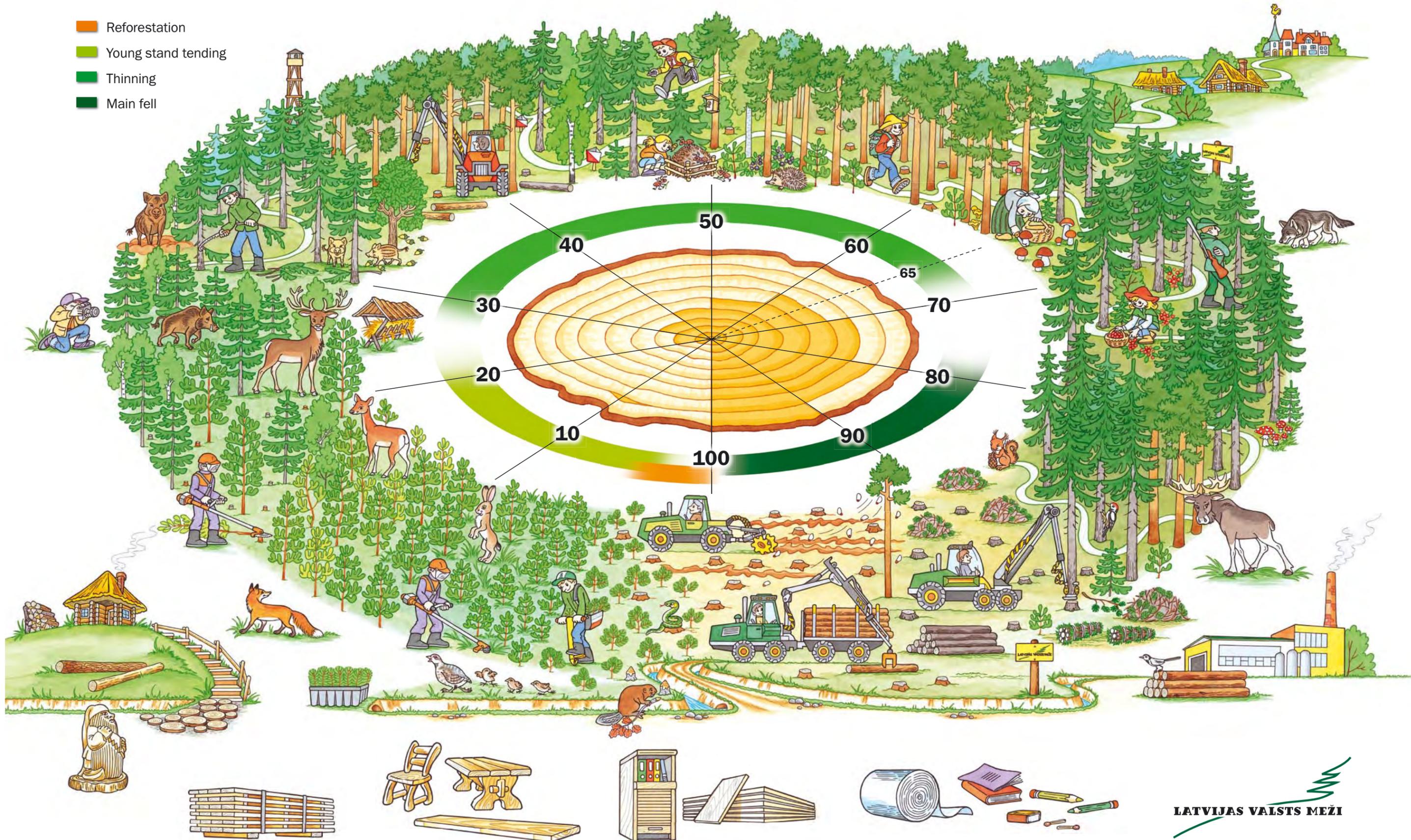
ЛОБЕСЕЛ ВУВУВ СЕНЕНЕЛ САСЕ

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Forest management cycle

- Reforestation
- Young stand tending
- Thinning
- Main fell



The state forest's capital value increased significantly in 2005 by continuing the previously started LVM forest road construction and renovation program. In 2005, 617 kilometers of new forest roads were built, which reduced the cost of transporting timber to main roads and, therefore, increased the value of this timber. It is also very important that the development and improvement of work at the LVM Plants and Seeds unit continued during 2005.

In 2005, LVM stated another significant project: research on the possibilities of producing chips from cutting waste (branches, tops and the like) that could be efficiently used to produce heating and electrical energy. This is nothing new in Europe, but in Latvia this procedure is still under development, and increasingly topical if one considers the systematic rise in the price of fossil fuels (gas, petroleum and coal).

In 2005, LVM conducted activities to educate society about processes in the forest, the significance of forests for the national economy and also undertook the extensive action "Don't Litter in the Forest" which got a great response from the public and will be continued in 2006. State forests in Latvia are open to any member of society, therefore LVM last year continued to improve recreational and educational areas of the state forests, starting from benches and bonfire sites at the forest's edge to walking and educational trails at significant natural and historical areas.



Finally, in assessing the work of LVM, one must conclude that efficient forest management, well-developed forest infrastructure and high quality plants (even Swedish forest owners have started buying LVM grown plants) will, in the future, ensure that the forestry sector has high quality timber and maximum income for the state from its forests, naturally, in compliance with the requirements of nature conservation, environmental protection and the interests of society.

MANAGEMENT

MANAGEMENT



January 8-9

The most powerful storm in the past 35 years strikes, uprooting or breaking 2.8 million m³ of timber in the forests administered by LVM. Already on January 10, cleanup work on storm damages began.

January 27

For the first time, LVM organized a public presentation and discussion of the final results of research funded the previous year (2004). LVM invested LVL 231 000 in 2005 for scientific research.

February 21-25

As part of the Latvian team (SO "Meža sports"), 19 LVM employees participated in the 37th European forest workers biathlon competition (EFNS) in Belarus. Inese Zvirgzdiņa from the Vidusdaugava and Jānis Kaimiņš of Ogre forestry technical high school won bronze medals. This was the largest number of medals won since Latvia started participating in the competition.



Forest Days 2005

April 23

The main event of Forest Days 2005 with the motto "The Forest – A Value for Everyone". LVM participates with its tent, offering visitors various educational and entertaining activities.

April 26

LVM participates in the founding of a national support group for the European Forest-Based Sector Technology platform. To more efficiently obtain EU financial support, with the aim of increasing the competitiveness of the forestry industry, this group drafted a strategic vision for the sector and participates in the proceedings of the common EU Forest-Based Sector Technology platform.

EVENTS OF 2005

EVENTS OF 2005

■ May 4

LVM, together with Olympic athletes Jānis Lūsis and Liene Sastapa and more than 100 young people from Projekts Pēdas (Project Footprints), started a new campaign in the state forests 1=2 by presenting the country with 2 ha of forest. The aim of this campaign is to demonstrate to the general public, how JSC "Latvijas valsts meži" replaces each felled tree by two newly planted ones.

■ May 13

The Tērvete nature park wins the "The Most Family Friendly Place in Latvia" – title in a competition organized by the Ministry of Child and Family Affairs. A majority of the Latvian public, which took part in the survey, listed Tērvete as the place in Latvia most pleasing and suitable for family recreation.

■ June 2

A large number of LVM employees (more than 100 people) visit the largest forestry industry exhibition in the world, *Elmia Wood*, in Jönköping, Sweden, to acquaint themselves with the newest forestry technologies.



■ The Tērvete recreation and nature park

■ June 6-10

LVM organizes the 6th conference of European state forest management organizations, during which the European State Forests Association EUSTAFOR is founded.

■ June 11

LVM employees participate in the rebirth of an ancient trade associated with the forestry industry, the Gauja river log floaters.

July 1

Taking into account the need for specialization in order to ensure quality of work, the subunit LVM Meža infrastruktūra (LVM Forest Infrastructure) is founded. Its purpose is to develop forest infrastructure – forest roads and drainage networks.

July 11-16

LVM, together with the organization Meža sports (Forest Sports), organizes a European forest workers orienteering competition (12th EFOL) in Ventspils. Around 400 forest related people and their families from 15 countries participated. LVM organized excursions for the competition participants, showing them the Latvian forest management cycle.

July 23-24

Teams from all subunits of LVM as well as teams from educational and administrative institutions in the forest industry, participated in the Forest Games, a sports and recreational event organized by the Western Vidzeme forestry district of LVM in Mārkulīči.



Don't Litter in the Forest

July 27

LVM starts an extensive campaign against littering the forests with household rubbish which involves the Environmental Protection Fund and several private enterprises.

August 22

To increase society's understanding of the forest and the processes that go on there, LVM and the Fund for Environmental Education signed a memorandum of cooperation on August 22, under which LVM started implementing a new environmental education program, "Learning about Forest" in the Latvian schools.

EVENTS OF 2005

EVENTS OF 2005

August 25

LVM Seeds and Plants organizes an international seminar on the latest forest plant growing technologies with participants from eight countries: Latvia, Lithuania, Estonia, Sweden, Denmark, Finland, Poland and Belarus.

September 16

LVM gains the recognition of the Employers' Confederation of Latvia for innovative entrepreneurship by being selected among three finalists for the LDDK 2005 annual prize "For Innovation in Entrepreneurship". This recognition was gained for its implementation of modern technology and the development of forest plant production.

September 19

In order to facilitate the development of an independent roundwood measurement system in Latvia, LVM participated in the founding of a "Wood Products Sellers Organization".



Forest cleanup assistance with Prime Minister Aigars Kalvītis

September 30

LVM organizes a forest cleanup as part of the campaign "Don't Litter in the Forest" to cleanup the forest along two kilometers of coastline near Engure.

Prime Minister Aigars Kalvītis, Minister of Environment Raimonds Vējonis, Minister for Children and Family Affairs Ainars Baštiks and Minister of the Interior Ēriks Jēkabsons participated in this cleanup and several cubic meters of various rubbish were collected.

October 3-6

A routine Forest Stewardship Council (FSC) audit takes place at four LVM forestry districts. No new remarks are made. This acknowledges that the management of the State forests in Latvia is being carried out according to the world's top forestry standard.

■ November 15

43 representatives from 23 countries participate in the General Assembly of the European Confederation of Woodworking Industries. During the conference, the delegates visit LVM and learn about state forest management in Latvia.

■ November 17

On the eve of Latvian Independence Day, LVM solemnly inaugurates an observation tower it built at the historic Ložmetējkalns battle site in the Tīrelpurvs bog. The 27 meter high panoramic observation tower offers an impressive view of the historically significant sites of the "Christmas Battles" by the Latvian Riflemen.

■ December 1

LVM, the State Forest Service of Latvia, and the Swedish Östra Götaland forest administration hold a concluding seminar for their joint project "Management of Natural Forest Biotopes in Latvia" (2003 – 2005). A hitherto unprecedented gap analysis evaluation of the forest's biological diversity was completed within the framework of the project.



■ Panoramic observation tower at the historic Ložmetējkalns battle site

■ November 30 – December 2

LVM starts a research project on the use of future fuels – biomass – for energy, learning about experience in other countries.

EVENTS OF 2005

EVENTS OF 2005



The hurricane and its impact on AS Latvijas valsts meži

On January 7–9, 2005, an active Atlantic cyclone brought hurricane level winds to both Northern Europe and the Baltic. As a result of the strong winds and flooding, more than 10 people lost their lives in Northern Europe. Latvia was affected by the southern edge of the cyclone, which means that the territory of Latvia was in the zone of maximum wind speed. The January storm did significant damage to Latvia's forests, uprooting or breaking around 16 000 hectares of standing forest. For the first time, the cleanup of a storm of this intensity was done under market economy conditions. The total amount of timber damaged by the January storm in Latvia according to expert opinion is 7.4 million cubic meters.

The AS "Latvijas valsts meži" unit LVM Roundwood Deliveries (LVM AP) made an enormous contribution to the storm cleanup, especially in its earliest phases, when, with the help of this unit, the company was able, immediately after the storm fellings, to start harvesting cuttings and the sale of timber. In a short time (January– March) LVM Roundwood Deliveries harvested and sold more than 0.5 million m³ storm-felled timber. By selling only standing (or fallen) timber at auction and to partners with long-term felling contracts, there was a real risk that the storm damage would not have been cleaned up during 2005, with all that would have implied. It must also be emphasized that LVM AP made a contribution immediately after the storm by clearing forest roads of fallen trees as well as clearing working areas with harvesting machines where fallen trees and debris created dangerous conditions for lumberjacks. This allows one to conclude that LVM AP must continue to develop rapidly, especially in the direction of cuttings for the purpose of tending.

Storm-damaged timber, if not collected in a timely manner, fosters the proliferation of pests, especially the European spruce bark beetle. In 2005, the population of these pests increased tenfold compared to 2004, but did not reach the threshold of mass proliferation. The spruce bark beetle proliferates in damaged timber, therefore the rapid removal of storm-felled trees from the damaged forests limited the spread of the forest pest. After earlier damaging stormfalls in 1967 and 1969, slow cleanups led to the mass proliferation of spruce bark beetles, causing the same amount of loss as was caused by the wind.

THE STORM

THE STORM

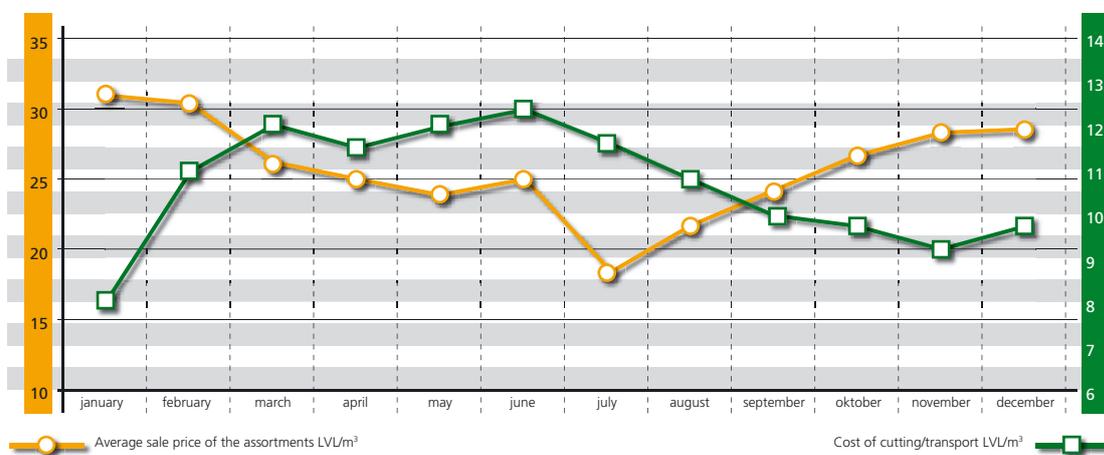
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In addition, during the spring of 2005, 1 100 pheromone traps and dispensers were used in the forests under LVM administration. The traps were placed in fresh spruce felling sites near the nesting areas of the previous year's spruce bark beetles. At present, the main task of forest protection is to ensure the supply of all necessary inventory and supplies for work in 2006 to limit the spread of the spruce bark beetle. There is a risk that, under favorable climat conditions, a mass proliferation could still occur, because in private forests preventive measures aren't being taken or are taken to an insufficient degree.

The storm-falls of January caused drastic changes in both the wood products market and the market for services related to wood products preparation and delivery. The mobilization of forest harvesting capacity, which was necessary to avert an ecological catastrophe and to reduce economic losses caused significant changes in demand for services, causing, as economic theory would dictate, a rise in the cost of these services. The nature of harvesting stormfalls and the productivity of this process in and of itself led to higher costs. In the area of timber transport, the price level of the Swedish market set Latvia's prices, because Latvian transporters literally divided their capacity between these markets. At the same time, on the wood products market, the buying power of sawmills was affected by the fall in wood product prices caused by the unprecedented rise in supply, causing overproduction in the market. As a result, timber transport vehicles were forced to spend hours in long lines at sawmills. As the harvesting of stormfalls ended, the situation gradually improved in the second half-year, as both wood product sales and payment for services returned to the contract prices that existed before the impact of the storm-falls on the market.

Average sale prices and cutting/transport cost on 2005





THE STORM 1967 – 1969

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A history of storm felling

Prof. Zigurds Saliņš

Powerful storms have stricken Latvia in the past. There is information that on June 10, 1795, a powerful whirlwind moved from the mouth of the Daugava River across Burtnieki and further on to Lake Peipus. The storm raged for four hours, accompanied by a thunderstorm and hail with hailstones weighing as much as 400 grams. The storm uprooted and broke trees of up to 50 cm in diameter. Almost a century later, on May 10, 1872, a whirlwind raged along a 70 kilometer swath from Bārta across Remte to Riga and beyond to Smiltene and Gaujiene. The forest areas around Allaži, Sigulda, Cēsis and Smiltene suffered especially heavy damage, but there is no information on the extent.

Less than 100 years passed and during the last century, the country was hit by two very powerful cyclones only two years apart.

The night of October 17 to 18, 1967, a powerful storm formed by two low-pressure systems over Denmark reached Latvia. Wind speeds were 30 m per second, with gusts of up to 45 m. The storm moved from Liepāja across Aizpute, Saldus and on to Jaunjelgava and Jēkabpils, where its force progressively diminished. This storm uprooted and broke around 12 million m³ of trees, which amounted to three years of planned felling. The worst hit were the Liepāja (2.3 million m³), Aizpute (0.8), Dobele (0.6), Jaunjelgava (1.0) and Jēkabpils (0.8) forest enterprise districts. Other Soviet-era forest enterprises suffered significant damage. The damage was mainly uprooting rather than broken trees, because the ground was wet at the time and not yet frozen. Deciduous trees still had their leaves, hence they suffered as much as conifers.

Immediately after the storm, all forestry enterprises stopped planned felling and concentrated all their efforts on clearing storm felled stands. Workers from less affected forestry enterprises were assigned to clearing storm falls, kolkhoz and sovkhos workers, as well as "volunteers" from other Soviet enterprises and organizations were recruited. This did not suffice, therefore workers were summoned from Belarus, the Ukraine and thinly forested parts of Russia. Some of them had no skills whatsoever in forest harvesting work and serious accidents were frequent occurrences. A large part of the timber was delivered to the " vast Motherland" and part of the immigrant labor remained permanently in Latvia.

The cleanup of the 1967 storm damage had not been completed, during the night of November 2, 1969 when another cyclone hit Latvia, coming from the Baltic Sea and the Bay of Riga. It struck hardest at the Alsunga (0.6 million m³), Ventspils (0.74), Ugāle (1.2), Dundaga (1.75) Kuldīga (0.7) Talsu (1.5), Tukums (1.0), Rīga (0.5), Inčukalns (0.65), Limbaži (1.0) and Salacgrīva (0.6) forestry enterprises. Further away from the sea in an easterly direction, the damage from the storm progressively diminished. All together, this storm uprooted or broke 14.4 million m³. During this storm fall, the deciduous trees had shed their leaves, therefore suffered less. New stands suffered the least, stands of medium age mainly were broken, but older stands were uprooted. This was because the trunks of mature stands were thicker and mechanically stronger, but their root systems often suffered from rot.

THE STORM 1967 – 1969



The total damage from both storms in state forests was around 26 million m³ 8 (including 19 million m³ of spruce trees). Adding insect damage, which resulted from long delays in the removal of storm falls, as well as the warm, dry summer and insufficient measures to combat the insects, the total losses in state forests were around 31 million m³.

To prevent forest fires, there was a ban on automobile traffic in the largest areas of storm damage during the time of highest fire danger and, in some places, there was a ban on entering the forest.

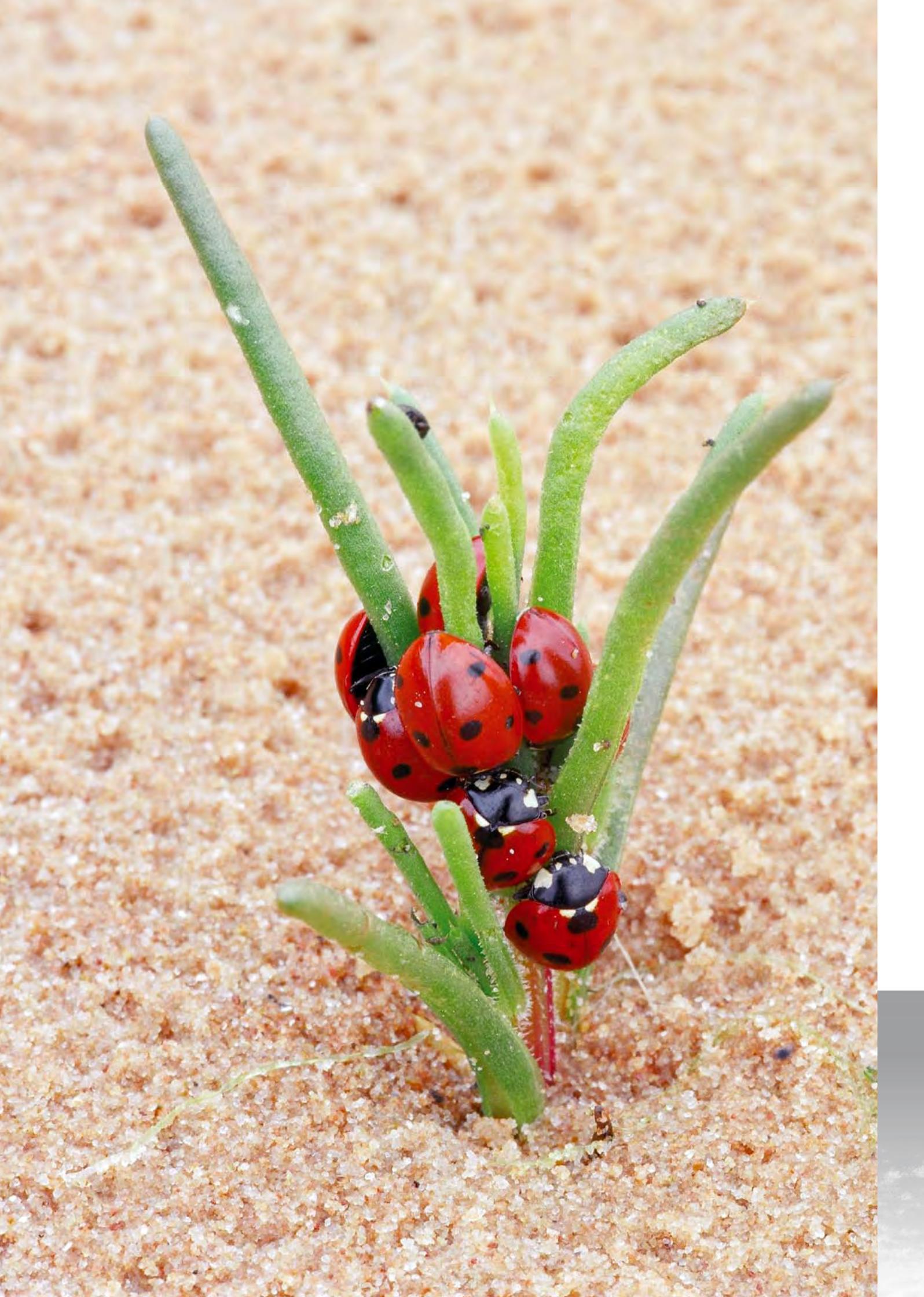
The harvesting of damaged stands and the transportation of the larger part of the resulting prepared timber was completed at the end of 1971, but removal of some clusters of storm felled trees, insect infested and dried trees, mainly from the edges of the damage area, continued until the fall of 1973.

It should be noted that during this time, in addition to the Ministry of Forestry and Forest Industry, various short-term administrative institutions were set up to coordinate the work of forestry workers from the other Soviet republics, leaving the division of the cuttings to the Ministry.

During the harvesting and processing of the storm felling, the morals and ethics of workers in the forestry sector suffered severely. During this time, representatives of kolkhozes in Russia and the Ukraine, as well as representatives of various black market "brigades" traveled around Latvia with suitcases of cash, trying to bribe officials of forestry enterprises to get the best cuttings as well as railway officials in order to get railroad cars to transport their timber to Russia and the Ukraine, especially to the Transcarpathian regions where there was a shortage of timber and its price was several times that in Latvia. There were people who gave their little finger to the "devil of money" only to lose an arm. Some forest workers significantly increase their personal wealth, but others, even high-ranking officials were caught and ended up behind bars.

The gang leaders of the black market enterprises, promised higher pay and recruited forestry enterprise workers and, by shady means, purchased or rented forest enterprise harvesting equipment, thereby reducing the production capacity of local enterprises.

THE STORM 1967 – 1969



A good LVM employee – satisfied with work and life

The purpose of LVM's personnel policies is to create conditions where employees are motivated not only by salary, social benefits, bonuses and performance-related incentives, but also by good working conditions, positive feedback for accomplishments, management responsibility toward employees, opportunities for career development, a healthy and safe working environment and positive relations among employees.

In order to implement these basic principles, a study of the company's corporate culture – the common values, working habits and norms of the employees – was completed and presented at the end of 2005.

The study shows that LVM has a task-oriented company, where all else is subject to meeting business goals and requirements. It is this collective way of thinking that has allowed us to optimally achieve business goals and ensure day-to-day progress. A second finding was "culture of cooperation," because management is aware of the significance of team cohesion for reaching good work results and has a high regard for the role of cooperation and internal communication on a day-to-day level. The impact of other kinds of corporate culture on LVM was not determined.

To use an allegory, the LVM staff could be compared to a good choir, which sings under a conductor and has a few soloists, but the individual notes they sing are not stronger or more impressive than their performance as a whole.

It was determined that LVM employees are ready for changes and even desire and support them, because they consider a changing work environment to be innovative and present an opportunity for development and learning. Both managers and employees are ready to expand or change their areas of responsibility in order to achieve better work results and have a well-ordered quality of working life.

Five important values have been determined at LVM, which employees consider significant for everyday work:

- Honesty
- Accomplishments and work results
- Competence
- Cooperation, friendliness and joviality
- Pride in one's organization

In the future, as well, personnel management will be based on recognizing that the level of business success depends on trustworthy, capable and motivated staff that is wholly committed to the development of LVM.

PERSONNEL MANAGEMENT

PERSONNEL MANAGEMENT



LVM manages environmental values of European significance

The aim of LVM in nature and environmental protection is to preserve biodiversity in the forests under its management and to preserve the forest ecosystem's role in the protection of soil, water and landscape.

What is Natura 2000?

All of the countries of the European Union have undertaken the formation of a common network of protected areas: Natura 2000. Since 2004, Latvia, too, has formed its part of the network, which was made from the already existing specially protected areas, adding 122 new ones. The precondition for forming an area is the protection of rare and threatened plant and animal species and their habitats. Lists of such species and habitats are included in two EU directives and ensuring their favorable and protected status is obligatory for all EU countries. 20 plant species, 20 invertebrates, 5 mammals, 3 reptiles, 11 fish species, 70 bird species and 60 kinds of habitats listed in the directives are present and protected in Latvia.

Natura 2000 areas in Latvia

The Natura 2000 network in Latvia includes 336 areas, 4 strict nature reserves, 3 national parks, 250 nature reserves, 38 nature parks, 9 protected landscape areas, 9 natural monuments and 23 micro reserves. Together, they make up 11.9 % of Latvia's area. These areas have differing protection and management regimes, from minimal restrictions in protected landscape areas to a complete ban on commercial activity in nature reserves.

LVM – a significant manager of environmental assets in Natura 2000 areas

LVM manages more than 250 Natura 2000 sites (nature reserves, nature parks, protected landscape areas and micro reserves) or 207 000 ha, which is 13 % of the forestland under the administration of LVM. In order to manage the Natura 2000 sites under its administration in accordance with their protective purposes, LVM each year drafts and implements nature conservation plans for these sites. In 2005, 20 nature reserve plans were drafted, protected habitats were tended, information booths and signs put up, and recreational areas were facilitated for site visitors.

LVM pays special attention and does long-term research with the purpose of ensuring a favorable protective status for the following species and habitats of European importance:

Freshwater pearl mussel (*Margaritifera margaritifera*)

Black stork (*Ciconia nigra*)

Wood Grouse (*Tetrao urogallus*)

9010* Western taiga,

9020* Fennoscandian natural old broad – leaved forest

NATURA 2000

NATURA 2000

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LVM ensures the management of the Natura 2000 areas with funds from the sale of timber, mostly from forests, which are managed for the purpose of harvesting timber. In several Natura 2000 areas, (the nature park Tērvete, the nature reserves Zebrus and Svētes lake, the Viķi mire), LVM offers recreational services. In all administered areas, the total investment by LVM in protection of environmental and natural assets was LVL 4.8 million, of which LVL 3.7 million of unrealized revenues from timber.

The basic business of the company, forestry, is significantly restricted on Natura 2000 forestlands. These restrictions are restrictions on forestry production (mainly the harvesting of timber).

Type of restriction on forestry activities	Forest manager				Total from forestland in Latvia	
	LVM		All others			
	Area, ha	%	Area, ha	%	Area, ha	%
Any activity	33 882	2.1	26 822	1.7	60 704	1.9
Main cutting	112 814	7.1	60 890	3.8	173701	5.4
Clear cutting	33 093	2.1	51 306	3.2	84 399	2.6
Other restrictions	27 299	1.7	80 886	5.1	108 185	3.4
Total	207 088	13.0	219 904	13.8	426 989	13.3

LVM – a partner in joint projects in Natura 2000 areas

LVM participates as a partner in the management of Natura 2000 areas in three European Commission LIFE – Nature financed projects: “Implementation of Mire Habitats Management Plan for Latvia”, “Protection and management of the Northern Gauja river valley” and “Lake Pape – Conservation, Preservation and Evolution”.

In 2005, LVM’s protected nature area increased by 8 140 hectares or 0.5 % for a total of 466 840 hectares of 28.8 % of the land under LVM stewardship.

Of the forest lands managed by LVM, 227 617 hectares or 14.1 % are areas for the preservation of biodiversity. No forestry activities or main cutting is planned for these areas, only measures that are necessary for the maintenance of biodiversity.

The goal of management of the remaining protected areas, 14.7 % of LVM’s forest lands is to ensure recreational and learning experiences in the forest for the public, at the same time protecting the environmental and scenic role of the forest. Economic activity in these areas is planned in accordance with the purposes of the protective regime for each area.

Areas whose main purpose is the provision of high quality timber comprise 71 % of the land under LVM management.



“Latvijas valsts meži” brīdina:

NEMĒSLO MEŽĀ!
PAR CŪKU PĀRVĒRTĪSIES!

RECREATION FACILITIES MAP

БЕСПЕВНОИ УСЛОВИЯ РИВБ

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Welcome to Latvia's State Forest!



Recreational sites, nature trails and places of interest

Northern Kurzeme Forestry (Phone: + 371 3237824)

- 1 The Liepniekvalka Caves
- 2 The Dundaga Hunter house
- 3 The Dundaga Castle and Park
- 4 The White Dune
- 5 The Bilavu Devils Boat - stacks of boulders on an ancient burial site
- 6 Kaltenes kalvas - piles of boulders
- 7 The Jūrkalne Bluff

Southern Kurzeme Forestry (Phone: + 371 3448067)

- 8 Lake Bezdzibena (Bottomless)
- 9 Remtes Park
- 10 The Dunika Conservancy Area and the Bog Trail
- 11 The Kalētu Forest Park
- 12 The Aizvīku Forest Park - a display of wooden sculpture

Zemgale Forestry (Phone: + 371 3007166)

- 13 Bird Watching Site in the Engure Nature Park
- 14 Trail to sea
- 15 Vecupe (Oxbow)
- 16 The Jaunmoku Castle
(Phone: + 371 3107125)
- 17 Kapiera lake
- 18 Ložmetējkalns and Tīrelpurvis - Memorial Sites of the WWI Christmas Battles; a watch tower
- 19 The Kartavkalna Nature Trail
- 20 Bramberģes recreation sites
- 21 Zebraus lake
- 22 Lielaucis lake
- 23 The Pokaiņi Forest
(Phone: + 371 3762334)
- 24 The Tērvete Nature Park
(Phone: + 371 3763385)
- 25 The Hare's Meadow

Central Daugava Forestry (Phone: + 371 5161540)

- 26 The Skaistkalne Karsts - a geomorphologic site
- 27 Berlīnes crossroads
- 28 The Skrīveri Arboretum - a collection of exotic trees and shrubs
- 29 The Koknese Park and Anīmuīža manor house
- 30 The Kalsnava Arboretum - the biggest collection of ornamental trees and shrubs in eastern Latvia.
(Phone: + 371 4826568, 28380280, 29233063)
- 31 The Ellītes Sulphur Spring
- 32 Raibā stabīna road
- 33 Ozolkalnu road



Western Vidzeme Forestry (Phone: + 371 4207114)

- 34 The Nīdrāju-Pīlkas Bog
- 35 The Skaņaiškals - the outcrops of sandstone on the Salaca, a display of wooden sculpture
- 36 Oleru forest trail
- 37 The Liepupe Castle Mound
- 38 The Augstrozēs Medieval Castle Mound
- 39 The Zilais (Blue) Hill
- 40 The Bank of the Līgatne River
- 41 Vērša hill
- 42 Lake Kaupēna

Eastern Vidzeme Forestry (Phone: + 371 4776532)

- 43 Recreation Site at the Gauja Bridge
- 44 The trail "What the wood lands have in store"
- 45 The Vijciems Vintage Cone Dryer
(Phone: + 371 26478620)
- 46 The Čertene Castle Mound
- 47 The Silva Arboretum of Exotic Trees and Shrubs
- 48 Cycling route
- 49 Lake Nīdrāja - recreation sites around the lake
- 50 The Jaunannas Forest Trail
- 51 The Līdene Memorial - a site where the Soviets executed the Latvian Army personnel in the summer of 1941
- 52 Kaļņa lake



Northern Latgale Forestry (Phone: + 371 4607161)

- 53 Lakes Kalna and Lazdaga
- 54 The Balvi Ancient Park
- 55 The Tirumnieku Trail
- 56 The Ančupānu Forest Park
- 57 Kovšu lake
- 58 Plisuma lake

Southern Latgale Forestry (Phone: + 371 5307102)

- 59 The Forest Fire Lookout Tower "Gustiņi"
- 60 The Gārsene Forest Park
- 61 Jersikas habitats trail
- 62 The Giant Boulder of Nīcgaļe
- 63 The Rušenais Castle Mound
- 64 Pīroļu oak woodland
- 65 The Conservation Area "Čertoks" (Devil's Lake)
- 66 Nature park Daugavas loki (Daugavas circle)
- 67 Svētes nature park and Eglukalns hills watch tower
- 68 The Silenes Nature Park, The Pērkules Precipice

- Recreational sites
 - Nature trails
 - Places of interest

Nationwide campaign "Don't Litter in the Forest!"

Surveys show that around 82 % of the population of Latvia uses the state forests for recreation and that the numbers of recreational users are steadily increasing. Unfortunately, the amount of litter in the forest increases every year and a/s "Latvijas valsts meži" (LVM) must spend increasing amounts of money for litter removal, which cost LVL 80 000 in 2004.

To try to solve the growing problem of littering and pollution of the forests and to change public attitudes toward littering, LVM in 2005 started a nationwide campaign "Don't Litter in the Forest!" The Ministry of Environment of the Republic of Latvia and the Ministry of Agriculture as well as the private waste management company a/s L&T Hoetika supported the campaign. Non-government organizations took an active part in the campaign, including the group "Clean Forests" (Tīri meži) and "Project Footprints" (Projekts Pēdas).

As a result, from July to October 2005, LVM carried out a major informative campaign across Latvia, using TV, radio and outdoor advertising to ask the public not to litter in the forest. A special character Pigman (Cūkmens) was created to personify those who litter the forest, to gain media attention and to meet with more than 7000 children at schools and summer camps. Pigman announced the Pigman prize for the best photograph of littering and pollution of the forest. A campaign homepage www.cukmens.lv (Latvian language only) was created and a toll-free phone line 8002852 (the last four digits spell cūka, the Latvian word for pig) opened for the public to report illegal rubbish dumping in the forest. The worst polluted places in the state forests have been cleaned up. In 2005, more than 6000 m³ of rubbish was removed from the forest.



Raimonds Vējonis, Minister of Environment, Mārtiņš Roze, Minister of Agriculture, Roberts Strīpnieks, Chairman of the Board of the JSC "Latvijas valsts meži", and Indra Petrēvica, Administrative Director of the JSC "L&T Hoetika" open the campaign "Don't Litter in the Forest!"

The largest volunteer forest clean up took place with the participation of Latvian Prime Minister Aigars Kalvītis and four government ministers who helped clean the seashore near Engure. Thanks to the great publicity and extent of the campaign, more than 50% of the Latvian public recognized Pigman at the end of 2005, according to a survey by the public opinion research organization SKDS. LVM, therefore, has succeeded in raising the issue of forest littering to the national level. However, that is only a start, a good start. To continue the campaign tradition and to continue changing public attitudes toward pollution of the forest with rubbish, Pigman returns in 2006.

"DON'T LITTER IN THE FOREST!"

"DON'T LITTER IN THE FOREST!"



General

The joint stock company "Latvijas Valsts Meži" (Latvian State Forests – LVM) administers and manages state-owned forests in a manner that ensures the preservation and increase of their value, as well as revenue to the forest owner – the state.

The sole shareholder in LVM is the state through the Ministry of Agriculture of the Republic of Latvia. The company's institutions of governance are the General Meeting, the Supervisory Board and the Managing Board. The highest decision-making authority is the General Meeting, which represents the shareholder, the Ministry of Agriculture. The LVM Supervisory Board, in the interests of the shareholder, oversees the work of the Managing Board, which is the highest executive body of the company between General Meetings. In 2005, the LVM Managing Board consisted of 6 members, the chairman of the Board and five Board members.

Activities during the reporting period

LVM administers and manages 1.62 million hectares of land in the Republic of Latvia, including 1.39 million hectares of forest. 71.2 % or 1.15 million hectares of the territories administered by LVM serve, as their main purpose the harvesting of high-quality timber. From 2000 to 2005, there has been a significant increase in the areas under LVM administration deemed protected nature reserves for various reasons: from 12.9 % (208 700 ha) to 28.8 % (466 800 ha). One of the company's long-term goals is to expand the forest area under management, therefore it was planned to acquire 3000 ha of land during the reporting period. In fact, 984 ha were acquired and at the end of the reporting period there were 1498 ha of forestland on the company's balance sheet. In accordance with a suggestion by the Bureau for Prevention and Combating of Corruption, an audit of the land purchase tender procedures was performed, therefore the land purchase tender was not completed and the land purchase plan was not fulfilled during the reporting period. The audit did not reveal any violations of the tender procedure.

During the storm of January 8 – 9, 2005, around 3 million m³ of standing trees were broken or uprooted in territories administered by LVM. The huge supply of storm-felled timber caused a dramatic drop in timber prices, which significantly affected the company's cash flow. Despite the storm, the 2005 budget and operational plans were fulfilled and the company's revenues exceeded those planned, totalling LVL 69.5 million, or 112 % of budget. The reporting period is the first year when sales of the round wood assortment exceeded half (52%) of total turnover.

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	Budget in accordance with decisions of the General Meeting March 1, 2005	Budget in accordance with decisions of the General Meeting July 19, 2005	Actual
	LVL '000	LVL '000	LVL '000
Revenue, of which from	71 374	61 974	69 481
Standing sales	35 300	25 900	30 665
Round wood assortment sales	34 010	34 010	36 380
Lease of hunting grounds	482	482	498
Recreation and hunting services	383	383	378
Sales of forest tree seeds	43	43	48
Sales of forest planting stock	381	381	410
Leasing of land	194	194	206
Other income*	181	181	177
Interest income	400	400	719
Costs, total:	37 603	42 393	40 415
Production costs	35 947	40 737	38 829
Administrative costs	1 655	1 655	1 586
Real estate tax	2 755	2 755	2 295
Profit before company income tax	31 017	16 827	26 772
Company income tax	4 653	2 524	3 824
Profit after taxes	26 364	14 302	22 948

*the sum of revenues and costs that are not directly related to the commercial operations of the company

In 2005, the joint stock company "Latvijas valsts meži" completely fulfilled its obligations to the forest owner, the state, paying the amount (dividends of LVL 12.4 million) as foreseen by the law "On the State Budget for 2005" and all taxes applicable to LVM (LVL 14.9 million).

At the initiative of the Latvian Ministry for Agriculture and in accordance with deductions allowed under the law "On Corporate Income Tax", LVM contributed LVL 290 000 to charitable organizations during the reporting period.

The top priority during the whole year was to eliminate the consequences of the storm. The amount of important work done during 2005 to increase the value of forest capital assets and to fulfill the commercial operations plan was as planned. In accordance with the methodology submitted to the shareholder (Phase 1 of the Long Term Management Plan for Forest Capital), the calculated value of forest capital administered by LVM increased by LVL 29.9 million as a result of forest regeneration and tending. An average target model included in the plan was used and work (forest regeneration and tending) was done accordingly. In 2005, 11 235 ha of forest were regenerated with the tree species, regeneration methods and technologies foreseen by the plan. 38 855 ha of forest were tended (tending of young stands and thinning) in accordance with the frequency and intensity set forth in the aforementioned plan. An additional 16 139 ha were thinned, removing uprooted and broken trees from areas stricken by the storm.

To increase the total length of the company's truck-accessible roads, 617 km of forest roads were built in 2005 at an investment of LVL 13.4 million and added to the company's assets.

During the reporting period, Phase II of the development of the forest tree nursery business was started with the construction of a storage and sorting facility to offer high quality planting stock for delivery in accordance with customer deadlines and to increase the value of the forest resources.

The joint project "Management of Natural Forest Biotopes in Latvia" by LVM, the State Forest Service, and the Swedish Östra Götaland forest administration was completed. A methodology was drafted and areas of natural forest biotope concentration were identified in accordance with it. This is a precondition for the long-term preservation of the habitats of rare species. LVM has gained new and complementary knowledge from the project as well as practical experience in nature conservation and its long-term planning.

A public information and opinion making campaign "Don't Litter the Forest" (Nemēslo mežā) was launched with a central character "Pigman" (Cūkmens). The campaign was executed through a combination of video spots in the mass media and outdoor advertisements in combination with an intensive public relations and media campaign.

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		Planned in accordance with decisions of the General Meeting March 1, 2005	Planned in accordance with decisions of the General Meeting July 19, 2005	Actual
Standing sales	million m ³	2,60	2,95	3,38
Round wood assortment sales	million m ³	1,29	1,29	1,4
Forest regeneration	'000 ha	10,3	10,3	11,2
Forest (young stand) tending	'000 ha	29,9	29,9	30,1
Expansion of forest cultivation areas	'000. ha	2,7	2,7	0,6
Renovation of forest drainage systems	'000 ha	13	13	8,6
Forest inventory	'000 ha	148,5	148,5	176,3
Forest road building	km	630	630	617
Inventory of natural assets	'000 ha	5,1	5,1	4,1
Registration of land in the Land Book	'000 ha	200	200	56

The surveying and registration of land in the Land Book has been significantly delayed because of poor quality work. As a result, work has been returned to those performing for the correction of deficiencies.

The expansion of areas for forest cultivation has been delayed because the elimination of storm damage was a priority and the process of transforming agricultural land has proven more time-consuming than previously planned. In addition, we were unable to execute plans to acquire an additional 3000 ha of land.

The development of the company

LVM has received the recognition of the Employers' Confederation of Latvia (LDDK) by becoming one of the finalists for the LDDK 2005 award "For Innovative Entrepreneurship". This recognition was given for the implementation and development of modern technology in the production of forest planting stock

With the goal of developing the IT support systems, a description was made of all business processes and detailed process flow charts were developed to serve the improvement of business processes.

The reorganization of the company by specialized functions, which started the previous year, continued during the reporting period, with the result that two units were created for the more efficient management of LVM's real estate holdings and for the improvement of the quality of design and building of forest roads.

To improve the efficiency of timber deliveries, reducing the cost of timber measurement, as well as to make the measurement process more transparent and prevent "competition by measurement", LVM participated in the founding of the Wood Products Sellers Association of Latvia and the formation of an independent measuring institution.

In accordance with the directions of research defined in the company strategy, yearlong and longer academic research contracts have been signed for research on the following matters:

- improvement of forest tree species productivity by breeding methods and evaluation of wood quality;
- possibilities for reducing fito and entomological risks;
- methods for determining the value of forest capital and the development of value-enhancing models for forest management;
- monitoring the condition of natural resources and methods for their management;
- use of forest resources for energy production, more efficient forest harvesting technologies and support for timber delivery logistics.

In accordance with contracts, reports have been publicly presented on academic research that has been done for LVL 231 000, they have received positive evaluations from the company's consultative scientific panel and the results of this research are being used for innovations in commercial operations.

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Financial risk management

LVM ensures its commercial operations in accordance with a long-term development plan by using financial resources at the disposal of the company. Financial management is conducted centrally within the company, and the level of liquidity fully ensures a timely meeting of all liabilities toward commercial partners and the state. Since almost all revenues, in view of the market where sales occur, (more than 99 %) are in Latvian lats, the exchange rate risk to the financial indicators of the company is minimal. During the reporting period, there has been a significant rise in accounts receivable, but this has not had an effect on the financial stability of the company, since the majority of receivables are short-term. The company's accumulated cash resources are placed in low risk short-term financial instruments by buying liquid securities and investment in bank deposits with the aim of stable return.

Participation in international activities

LVM was one of the founders of the European State Forests Association (EUSTAFOR), which will serve as a lobbying organization at the institutions of the European Union (EU)

In 2005, the 6th European State Forest conference was successfully organized in Latvia by LVM. Delegates from state forest management companies and organizations in 23 European countries participated.

To achieve the European Forest-Based Sector Vision for 2030, a European Forest-Based Sector Technology platform was formed. To support this platform, a Latvian forest sector national support group was formed with the participation of LVM. The group's work has resulted with integration into the EU organization and the formulation of a draft national vision for 2030.

Developments after the end of the reporting period

In the time between the last day of the reporting period and the signing of this report, there have been no noteworthy developments that could significantly affect the operations of the company.

Main targets for 2006

- Achieve results in all directions of commercial operations in accordance with the annually reviewed five-year long-term development plan for each direction.
- To create and implement an efficient forest management planning system.
- To start the production of new products from cutting waste in order to use biomass for energy.
- To offer to the market container plants and bare-root plants with an improved root system comprising 58 % of all LVM sales of planting stock
- To achieve the increase in recreational and hunting services foreseen by the long-term development plan. the fire-damaged tourist and recreation center "Ezernieki" and the tourist and recreation center "Spāres" will be delivered for use.

Profit and Loss Account for the year 2005

	2005	2004
	Ls	Ls
Net sales	68,777,493	65,296,671
Cost of sales	(37,708,721)	(22,551,500)
Gross profit	31,068,772	42,745,171
Selling expenses	(449,933)	(163,445)
Administrative expenses	(2,231,950)	(1,796,183)
Income from other commercial activity	280,449	134,021
Other interest and similar income	718,531	1,059,799
Interest expenses and similar expenses	(294,843)	(16,801)
Profit before taxes	29,091,026	41,962,562
Company income tax	(3,690,698)	(5,755,860)
Changes in deferred tax	(133,512)	(101,830)
Other taxes	(2,318,970)	(2,176,432)
Profits for the year	22,947,846	33,928,440



Roberts Stripnieks,
Chairman of the Board

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Balance sheet as at 31 december 2005

	31.12.2005.	31.12.2005.
	Ls	Ls
Assets		
Long-term investments		
Intangible long-term assets	189,689	187,866
Fixed assets	37,936,365	22,848,856
Long-term financial investments	1,388,320	1,139,960
Total long-term investments	39,514,374	24,176,682
Current assets		
Stock	2,394,573	1,405,472
Debtors	7,740,151	2,134,934
Securities and participating interest	9,963,604	25,262,111
Cash and bank	5,186,813	945,904
Total current assets	25,285,141	29,748,421
Total assets	64,799,515	53,925,103
Liabilities		
Shareholders' funds		
Share capital	32,063,259	10,633,573
Impact of change of the accounting policy	103,996	–
Profit of the reporting period	22,947,846	33,928,440
Total shareholders' funds	55,115,101	44,562,013
Provisions	2,711,429	1,989,492
Creditors		
Long-term creditors	22,854	22,854
Short-term creditors	6,950,131	7,350,744
Total creditors	6,972,985	7,373,598
Total liabilities	64,799,515	53,925,103



Roberts Stripnieks,
Chairman of the Board

AUDITORS' REPORT

To the Shareholder
of joint stock company "Latvijas valsts meži"

We have audited the financial statements of joint stock company "Latvijas valsts meži" (hereinafter – the Company) for the year ended 31 December 2005, from which the condensed financial statements of the Company were derived, in accordance with International Standards on Auditing issued by the International Federation of Accountants. In our auditors' report dated 21 March 2006 we expressed an unqualified opinion on the financial statements of the Company for the year ended 31 December 2005, from which the condensed financial statements were derived.

We conducted our audit in accordance with International Standards on Auditing issued by the International Federation of Accountants. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the accompanying condensed financial statements are consistent, in all material respects, with the financial statements of the Company for the year ended 31 December 2005 from which they were derived.

For a better understanding of financial position of the Company as of 31 December 2005 and the results of its operations for the year then ended and of the scope of our audit, the accompanying condensed financial statements should be read in conjunction with the financial statements of the Company for the year ended 31 December 2005, from which the condensed financial statements were derived, and our audit report thereon.

Ernst & Young Baltic SIA
License No. 17



Diāna Krišjāne
Personal ID code: 250873-12964
Chairperson of the Board
Latvian Sworn Auditor
Certificate No. 124

Rīga, 24 May 2006

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LVM Sēklas un stādi (LVM Seeds and Plants)
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Madonas raj., LV-4860
Phone/Fax: (+ 371) 4826568

LVM Apaļkoksnes piegādes (LVM Roundwood Deliveries)
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Phone: (+ 371) 7805075

LVM Rekreācija un medības (LVM Hunting and Recreation)
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LVM Meža infrastruktūra (LVM Forest Infrastructure)
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