North American Development Bank
Banco de Desarrollo de América del Norte

2017 ANNUAL REPORT

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TRANSMITTAL
LETTER

April 2018

We are pleased to provide the 2017 Annual Report of the North American Development Bank (NADB), which presents NADB's continued success in meeting its mandate through the operations and activities undertaken during the year for the development and financing of environmental infrastructure projects benefiting the citizens of the U.S.-Mexico border region.

This annual report is comprised of two sections. Consistent with the requirements of Article VII, section 4(b), of the Charter, the first section covers annual environmental and operational results of the merged institution, including those reported by the Chief Environmental Officer (CEVO). The second section, consistent with the requirements of Article VII, section 4(a), of the Charter, contains the financial report, which includes the consolidated financial statements of NADB for the years ended December 31, 2017 and 2016, with an unqualified opinion issued by the independent auditor, Ernst & Young LLP, along with management's discussion and analysis of the most relevant financial, lending and operating activities for the past fiscal year.

On November 10, 2017, the merger of NADB and the Border Environment Cooperation Commission (BECC) was completed by amendments to the Charter establishing both institutions. In anticipation of the legal formalities, NADB and BECC had been working under an operational merger that was quite useful in defining organizational structures and in preparing for formal approval. While the environmental mandate and geographic jurisdiction of the merged institution remain unchanged, the integration of the functions of BECC into NADB strengthens its ability to carry out its mission. All phases of the project cycle—from development and certification through implementation and closeout—have now been incorporated and streamlined within NADB, making more efficient use of available resources and improving service to border communities.

Under the new structure of the merged institution, the role of the CEVO was established for the purpose of reinforcing and ensuring the environmental integrity of all the operations of the Bank, as well as endorsing all projects under consideration for certification and possible financing.

During the integration process, NADB continued its successful record of financing environmental infrastructure in the border region, while operating in a strong and financially sound manner. In 2017, ten new projects were approved with financing totaling US$288.4 million, while US$113.9 million in loans and grants were disbursed for the execution of 30 projects in implementation, with more than half of those projects in the water and wastewater sector. Moreover, 11 projects were completed, including a cogeneration facility with the capacity to supply part of the electricity to operate a wastewater treatment plant in Ciudad Juarez, Chihuahua, and improvements to an irrigation system that is preventing an estimated 747 million gallons a year of water losses from seepage and spillage for farmers in Hidalgo County, Texas.

In the area of technical assistance and capacity building, US$1.17 million in grants were approved through the Technical Assistance Program (TAP) to fund 18 studies, training seminars and other development activities. Prior to the institutional merger, BECC also administered US$1.36 million in grants provided by the U.S. Environmental Protection Agency (EPA): US$1.03 million approved through the Project Development

Assistance Program (PDAP) and US$334,615 derived from the U.S.-Mexico Border 2020 Program. As part of its ongoing technical assistance efforts, NADB will continue to pursue partnerships with other entities aimed at creating synergies that support the development of environmentally sustainable and resilient border communities.

The North American Development Bank wishes to acknowledge and thank its many partners in the border region for their support during this transition phase. Bank management and staff are excited about this new chapter in the operation of the Bank and look forward to working on new opportunities to continue improving environmental conditions and provide a better quality of life for residents along the U.S.-Mexico border.

Alex Hinojosa
Managing Director

Calixto Mateos-Hanel
Deputy Managing Director

Salvador López-Córdova
Chief Environmental Officer

MANDATE
AND GOVERNANCE

MANDATE

NADB is a binational financial institution established and capitalized by the Governments of the United States and Mexico for the purpose of financing infrastructure projects that preserve, protect or enhance the environment in order to advance the well-being of border residents, as well as providing technical and other assistance to support the development of such projects. The scope of the Bank's mandate—including the geographic jurisdiction and infrastructure sectors in which it may operate—as well as its functions and limitations, are defined in an agreement between the two governments (the Charter).

Projects that qualify as eligible infrastructure are those that will prevent, control or reduce environmental pollutants, improve the drinking water supply or protect flora and fauna, provided that such projects also improve human health, promote sustainable development or contribute to a higher quality of life. In addition, eligible projects must be located within 100 kilometers (about 62 miles) north of the U.S.-Mexico international boundary in the U.S. states of Texas, New Mexico, Arizona and California and within 300 kilometers (about 186 miles) south of the border in the Mexican states of Tamaulipas, Nuevo Leon, Coahuila, Chihuahua, Sonora and Baja California.

ELIGIBLE SECTORS AND PROJECTS

WATER
Potable water supply, treatment and distribution; wastewater collection, treatment and reuse; water conservation; storm drainage and flood control

WASTE MANAGEMENT
Sanitary landfills, dumpsite closure, collection and disposal equipment, recycling and waste reduction, hazardous waste treatment & disposal facilities, industrial site remediation

AIR QUALITY
Street paving and other roadway improvements; public transportation; ports of entry, reduction of industrial emissions; methane capture

CLEAN AND EFFICIENT ENERGY
Solar, wind, hydroelectric, geothermal, biogas & biofuels; equipment replacement, building retrofits

BASIC URBAN INFRASTRUCTURE
Projects that consist of a mix of works from various sectors, such as street paving, installation of water and sewer lines, storm drainage and public lighting

BOARD OF DIRECTORS

NADB is governed by a ten-member Board of Directors with equal representation from each member country. The chairmanship alternates between the United States and Mexico each year. All powers of NADB are vested in the Board of Directors, which determines policy within the framework of the Charter and approves all programs and project proposals of the Bank.

MEXICO	UNITED STATES
◆ Secretary of Finance and Public Credit (SHCP)*	◆ Secretary of the Treasury
◆ Secretary of Foreign Relations (SRE)	◆ Secretary of State
◆ Secretary of Environment and Natural Resources (SEMARNAT)	◆ Administrator of the Environmental Protection Agency (EPA)
◆ Mexican border state representative	◆ U.S. border state representative
◆ Mexican border resident representative	◆ U.S. border resident representative

* Board chair, 2017

BOX 1:
PROFILE OF NADB UNDER AMENDED CHARTER

ENVIRONMENTAL MANDATE	**Continues**	NADB remains dedicated to providing financing to support the development and implementation of environmental infrastructure projects, as well as providing technical and other assistance for projects and actions that help preserve, protect and enhance the environment of the border region in order to advance the well-being of the people of the United States and Mexico.
GEOGRAPHIC SCOPE	**No change**	NADB jurisdiction is still defined as the region 100 km north and 300 km south of the U.S.-Mexico border.
BOARD OF DIRECTORS	**No change**	The ten-member Board of Directors that governed the two separate institutions remains the same, ensuring the continuity of the mission and functions of the two entities under NADB.
ORGANIZATIONAL STRUCTURE	**Strengthened**	The position of chief environmental officer (CEVO) was created to verify the environmental integrity of all projects and their compliance with the certification criteria, as well as to help identify new areas of environmental infrastructure needs. BECC personnel were incorporated throughout the structure of the Bank, consolidating its environmental and technical expertise and reinforcing the continuity of the functions developed at BECC. Operationally, project departments were realigned by financing type. In the case of all grant-funded projects, one department is responsible for the complete development cycle, from certification through closeout. For loan-funded projects, two departments continue to split these same responsibilities, with one dedicated to project development and financial services and the other to project implementation and loan administration.
SERVICES AND PROGRAMS	**Strengthened**	NADB continues to certify projects for loan and grant financing, as well as provide technical assistance and other support for project development; however, the redundancy of two entities performing many of the same tasks separately has been eliminated. Public participation, transparency and access to information also continue to be central to all operations.
OFFICES	**No change**	The current offices in San Antonio, TX, and Ciudad Juarez, CHIH, will continue to serve the border region.

BANK ORGANIZATION

MANAGEMENT TEAM	
MANAGING DIRECTOR	Alex Hinojosa
DEPUTY MANAGING DIRECTOR	Calixto Mateos-Hanel
CHIEF ENVIRONMENTAL OFFICER	Salvador López-Córdova
DIRECTORS	
CHIEF FINANCIAL OFFICER	Héctor Camacho
GENERAL COUNSEL	Lisa A. Roberts
DIRECTOR OF RISK MANAGEMENT AND CONTROL	Bernardo Salas
DIRECTOR OF INFRASTRUCTURE FINANCING AND FINANCIAL SERVICES	Carlos Carranza
DIRECTOR OF PROJECT AND LOAN ADMINISTRATION	Rafael Escandon
DIRECTOR OF GRANT FINANCING	Renata Manning-Gbogbo
DIRECTOR OF TECHNICAL ASSISTANCE	Mario Vázquez
DIRECTOR OF PUBLIC AFFAIRS	Jesse J. Hereford
DIRECTOR OF ADMINISTRATION	Eduardo Macias

SECTION 1
ENVIRONMENTAL & OPERATIONAL RESULTS REPORT

NOTE

This section of the Annual Report also includes information and figures related to activities carried out by BECC prior to the merger with NADB. In particular, the Project Development Assistance Program (PDAP) and the U.S.-Mexico Border 2020 Program were administered by BECC until November 10, 2017, the date on which the institutional integration went into effect. For that reason, the financial figures reported for those programs in this section are not reflected in the finances of the Bank.

NEW PROJECTS
APPROVED

Ten new projects were approved for NADB financing, of which US$283.2 million was in loans and US$5.2 million in grants. The total investment for the 10 projects is estimated at US$1.07 billion.

	PROJECTS CERTIFIED	LOCATION	POPULATION TO BENEFIT	FUNDING APPROVED	
				Type*	Amount (US$ Millions)
WATER AND WASTEWATER					
1	Cuadrilla Wastewater Collection and Treatment Project	El Paso County, TX	85	Grant	$ 1.80
2	Wastewater Collection Project	Loma Blanca, CHIH	4,933	Grant	0.63
3	Wastewater Infrastructure Project	Marathon, TX	546	Grant	1.55
4	Water and Wastewater System Expansion and Improvements	San Luis Rio Colorado, SON	70,064	Loan	10.05
5	Rehabilitation of the Collector Poniente	Tijuana, B.C.	86,950	Grant	1.17
CLEAN ENERGY					
1	Santa Maria Solar Park Project	Galeana, CHIH	195,340	Loan	55.50
2	Vicente Guerrero Wind Energy Project	Güémez, TAM	224,287	Loan	30.00
3	Orejana Solar Park Project	Hermosillo, SON	175,417	Loan	50.00
4	El Mezquite Wind Energy Project	Mina, N.L.	432,965	Loan	105.00
5	Rocksprings Wind Farm	Val Verde County, TX	138,399	Loan	32.69
	Total		**1,328,986**		**$ 288.39**

* All grants were awarded through the Border Environment Infrastructure Fund (BEIF), funded by the U.S. Environmental Protection Agency (EPA) and administered by NADB.

MAIN BENEFITS
ANTICIPATED

WATER & WASTEWATER

FIRST-TIME ACCESS TO SERVICE → **12,976 households** with sewer service and **582 households** with water service

NEW OR IMPROVED SEWER SYSTEM → **136 miles** of pipeline to be installed or replaced, directly benefitting an estimated 99,638 residents

WASTEWATER FLOWS TO BE COLLECTED → **7.6 million gallons a day** of sewage is expected to be collected and safely conveyed to treatment plants

CLEAN & EFFICIENT ENERGY

NEW GENERATION CAPACITY → **780 megawatts** to be installed through three wind farms and two solar parks

ELECTRICITY TO BE PRODUCED → **2.66 gigawatt-hours** in the first year of operation, sufficient to supply power to about 331,300 households

EMISSIONS TO BE PREVENTED → **1.26 million metric tons of carbon dioxide**, equivalent to removing 270,500 passenger vehicles from circulation

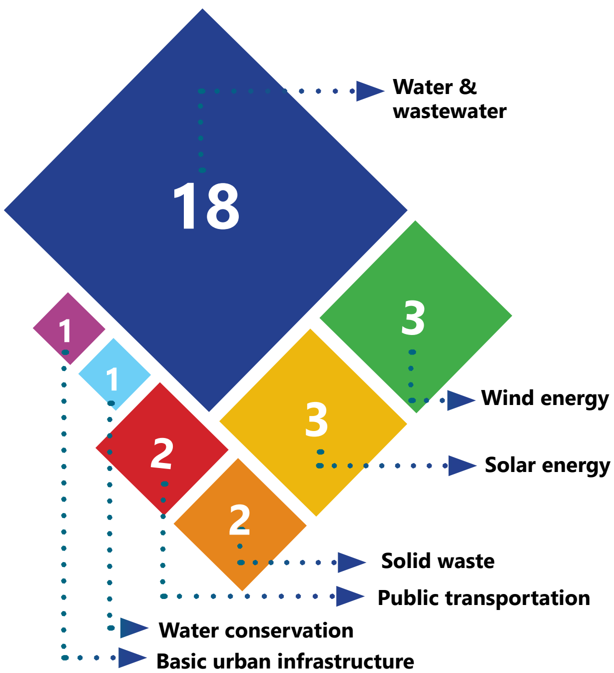
FINANCING
ACTIVITY

New financing totaling US$288.4 million was approved for 10 new projects, along with US$1.1 million in additional grant funding for two projects certified previously; financing agreements totaling US$245.6 million were signed with the sponsors of 13 projects; and US$113.9 million in loans and grants was disbursed to support 30 projects in various stages of implementation.

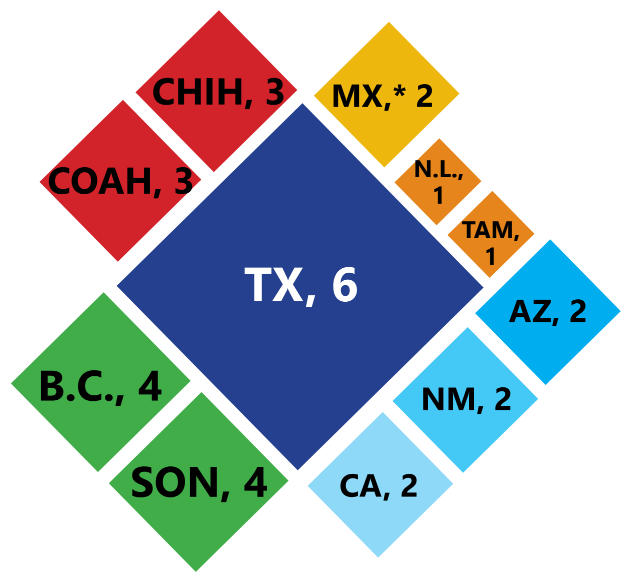
Disbursements were spread across all ten border states within the geographic jurisdiction of the Bank in 2017. As a reflection of the higher cost of energy projects, 64.1% of the funds disbursed went to support three wind farms in Coahuila, Nuevo Leon and Texas. However, in terms of the number of projects funded, 60.0% were in the water and wastewater sector in nine states.

DISBURSEMENTS

HOW FUNDING WAS USED
(No. of projects)



WHERE FUNDING WAS INVESTED
(No. of projects)



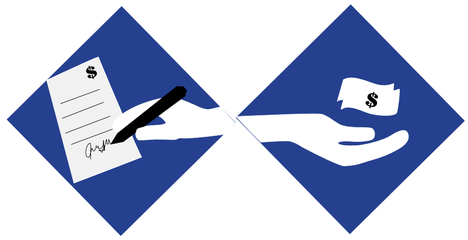
* MX = Border-wide programs in Mexico, with current participants from Baja California, Chihuahua, Nuevo Leon and Sonora.

FINANCING
SOURCES

In addition to offering market-rate loans and other financial services to project sponsors, with the approval of its Board of Directors, NADB uses a portion of its retained earnings to finance critical environmental infrastructure projects in low-income communities with grants through the Community Assistance Program (CAP). NADB also administers grant funds provided by the U.S. Environmental Protection Agency (EPA) through the Border Environment Infrastructure Fund (BEIF) for the implementation of priority water and wastewater projects located within 100 kilometers of both sides of the U.S.-Mexico border.

While most of the financing provided by NADB is in the form of loans, grants continue to provide crucial support for public services, especially in small communities that do not have the capacity to incur debt to address all their infrastructure needs. Financing activity and results by program are highlighted below.

2017 FINANCING RESULTS BY PROGRAM



LOAN PROGRAM

US$283.2 MILLION APPROVED → for six new projects certified during the year: three wind farms, two solar parks and one water and wastewater project

US$229.5 MILLION CONTRACTED → with the sponsors of three projects in the U.S. and four projects in Mexico

US$101.4 MILLION DISBURSED → to support 11 projects in implementation, including additional disbursements under the revolving credit lines for two low-emission bus programs

US$1.29 BILLION → in outstanding loans at year-end

COMMUNITY ASSISTANCE PROGRAM (CAP)

US$1.5 MILLION CONTRACTED → with the sponsors of two solid waste projects in Mexico and a water project in the U.S.

US$979,685 DISBURSED → to support the implementation of five projects

BORDER ENVIRONMENT INFRASTRUCTURE FUND (BEIF)*

*Funded by EPA and administered by NADB

US$5.1 MILLION APPROVED → for four new projects certified during the year, along with US$1.1 million in additional funds for two projects approved in prior years

US$14.5 MILLION CONTRACTED → with the sponsors of two projects in the U.S. and one project in Mexico

US$11.3 MILLION DISBURSED → to support 13 projects in construction

A more detailed analysis of NADB financing activity and results is provided in the Financial Report, which is presented in Section 2 of this document.

PROJECT IMPLEMENTATION

During the course of the year, work began on 16 projects, including:

- Two wastewater treatment plants with a combined capacity of 1.6 million gallons a day in Arizona and New Mexico;
- Five solid waste equipment projects benefiting 13 Mexican communities in Chihuahua and Coahuila; and
- Four renewable energy projects that will add 630 megawatts of generation capacity to the Mexican electricity grid.

Two border-wide financing programs for the purchase of low-emission buses established in Mexico in 2014 and 2016 also continued operation with 59 vehicles financed in 2017. Of those vehicles, 47 were new diesel buses that at a minimum comply with Mexican emission standards equivalent to those established by EPA in 2004 and 12 were compressed natural gas fueled buses that comply with the equivalent of EPA 2013 emission standards.

By year end, 11 projects had completed construction and begun operation in the water and clean energy sectors. Highlights of those projects, as well as more detailed information about each project, is provided on the following pages.

PROJECT IMPLEMENTATION ACTIVITY IN 2017	
Projects in process at beginning of year	32
Projects initiated	16
Projects completed	11
Projects in process at end of year	38

COMPLETED PROJECTS
NOW IN SERVICE

11 projects representing a total investment of US$872.02 million and benefitting more than 655,000 border residents began operation.

WATER & WASTEWATER

3 WATER SYSTEM IMPROVEMENT PROJECTS → including an **arsenic removal facility** with the capacity to treat **864,000 gallons a day** of well water, reducing arsenic concentrations to permitted levels

1 WATER CONSERVATION PROJECT → reducing water losses from seepage and spillage by an estimated **746 million gallons a year** and energy consumption by an estimated **62,000 kilowatt-hours a year**

1 WASTEWATER TREATMENT PLANT → with the capacity to treat **850,000 gallons a day** wastewater was rehabilitated, significantly improving the quality of the treated water discharged to surface water bodies in California

CLEAN & EFFICIENT ENERGY

1 COGENERATION FACILITY → installed with the capacity to supply between **40% and 50% of the electricity needs** of the wastewater plant, using the biogas produced from treated sludge

3 WIND FARMS AND 2 SOLAR PARKS → with a combined generation capacity of **417 megawatts**, which are expected to produce 1.57 gigawatt-hours of electricity in their first full year of operation, thereby preventing the emission of **805,400 metric tons of carbon dioxide** from conventional fossil fuel-based power plants, the equivalent of removing 172,463 passenger vehicles from circulation

GENERATING
SAVINGS FROM WASTE BYPRODUCTS

SOUTH WASTEWATER TREATMENT PLANT COGENERATION AND IMPROVEMENTS PROJECT
Ciudad Juarez, Chihuahua
Loan: US$2.77 million
Completed: May 2017

"It's one of those projects that mark a new era in the sustainable operation of the plants."

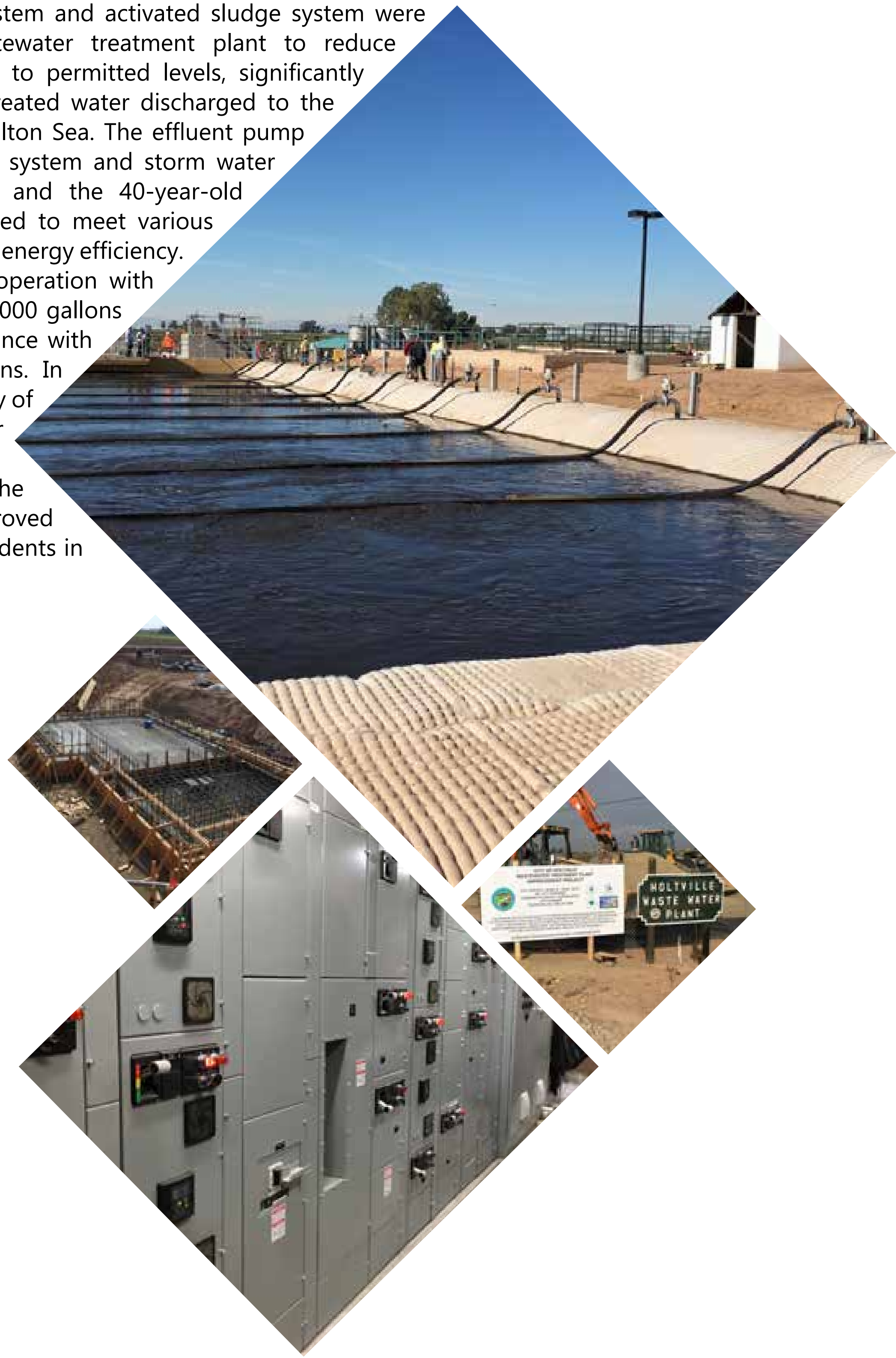
– **Oscar Fidencio Ibáñez Hernández**
Chairman of the Board of the Chihuahua state water agency, *Junta Central de Agua y Saneamiento de Chihuahua* (JCAS)

A 1.35-megawatt cogeneration facility was installed to supply up to half of the electricity needed to operate the South Wastewater Treatment Plant (WWTP), which consumed almost 15.46 gigawatt-hours (GWh) in 2017. Using the biogas produced in the treatment process, the facility has the capacity to generate an estimated 7.43 GWh of electricity annually. During its first five months of operation in 2017, the plant generated 1.07 GWh. In addition, as part of the project, two centrifuges were installed in 2015 to replace the belt-filter presses in the sludge dewatering process, which can remove up to 60% more water content, reducing the volume of biosolids deposited in the municipal landfill. With the new equipment, the volume of dehydrated sludge was reduced by 38,885 cubic yards in 2016, more than twice the annual amount originally projected (17,426 cubic yards).

IMPROVING
EFFLUENT QUALITY

WASTEWATER TREATMENT PLANT IMPROVEMENTS
Holtville, California
BEIF Grant: US$6.89 million
Completed: May 2017

A BIOLAC® wave oxidation system and activated sludge system were installed in the existing wastewater treatment plant to reduce ammonia and other pollutants to permitted levels, significantly improving the quality of the treated water discharged to the Pear Drain, Alamo River and Salton Sea. The effluent pump stations, ultraviolet disinfection system and storm water tanks were also rehabilitated, and the 40-year-old operations building was replaced to meet various code requirements and improve energy efficiency. The upgraded plant is in full operation with the capacity to treat up to 850,000 gallons a day of wastewater in compliance with all federal and state regulations. In addition to improving the quality of groundwater and surface water resources for the protection of aquatic ecosystems in the area, the upgraded plant is providing improved wastewater service to 6,600 residents in and around the city.



ENSURING
DRINKING WATER QUALITY

WATER SYSTEM IMPROVEMENTS PROJECT
Mesilla, New Mexico
BEIF Grant: US$698,115
Completed: April 2017

Three new waterlines were constructed to provide network looping in the water distribution system, improving water quality for 1,450 residents living in and around Mesilla. The new looping system has eliminated dead ends in the water system where water may stagnate, requiring additional operation and maintenance work to disinfect and flush the lines, resulting in water losses and increased costs. A total of 7,621 feet of polyvinyl chloride (PVC) pipeline was installed, including first-time service access for 15 homes in outlying areas of the city. Prior to the project, those homes relied on private wells for drinking water; however, during periods of extended drought, the wells could go dry, forcing residents to haul water, which may pose a health risk if the containers are not properly handled.

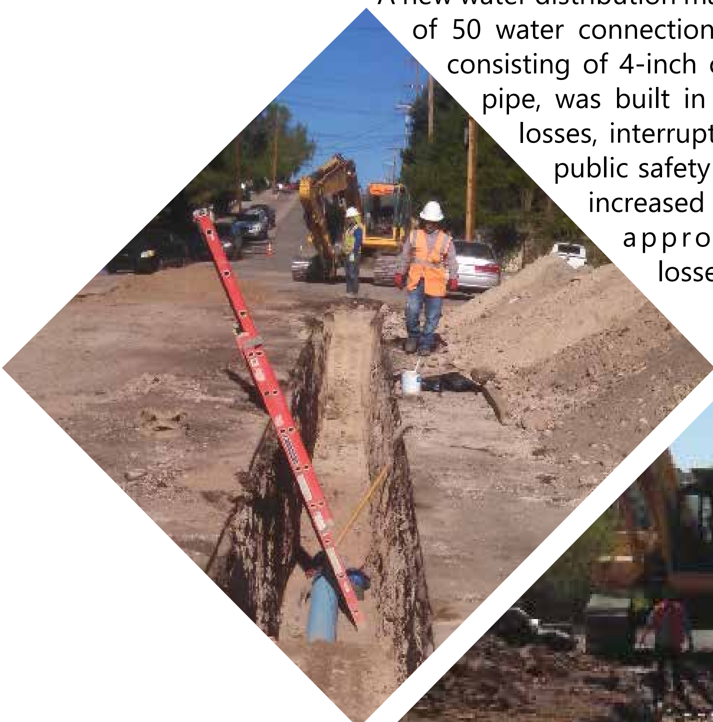
> *"We have residents that are already coming in, going through the process of hooking up to the utility. We're working with them on a case-by-case basis, because it is a little expensive for some of them, but they are very anxious to get on to the system."*
>
> – **Nora Barraza**, Mayor of Mesilla, NM

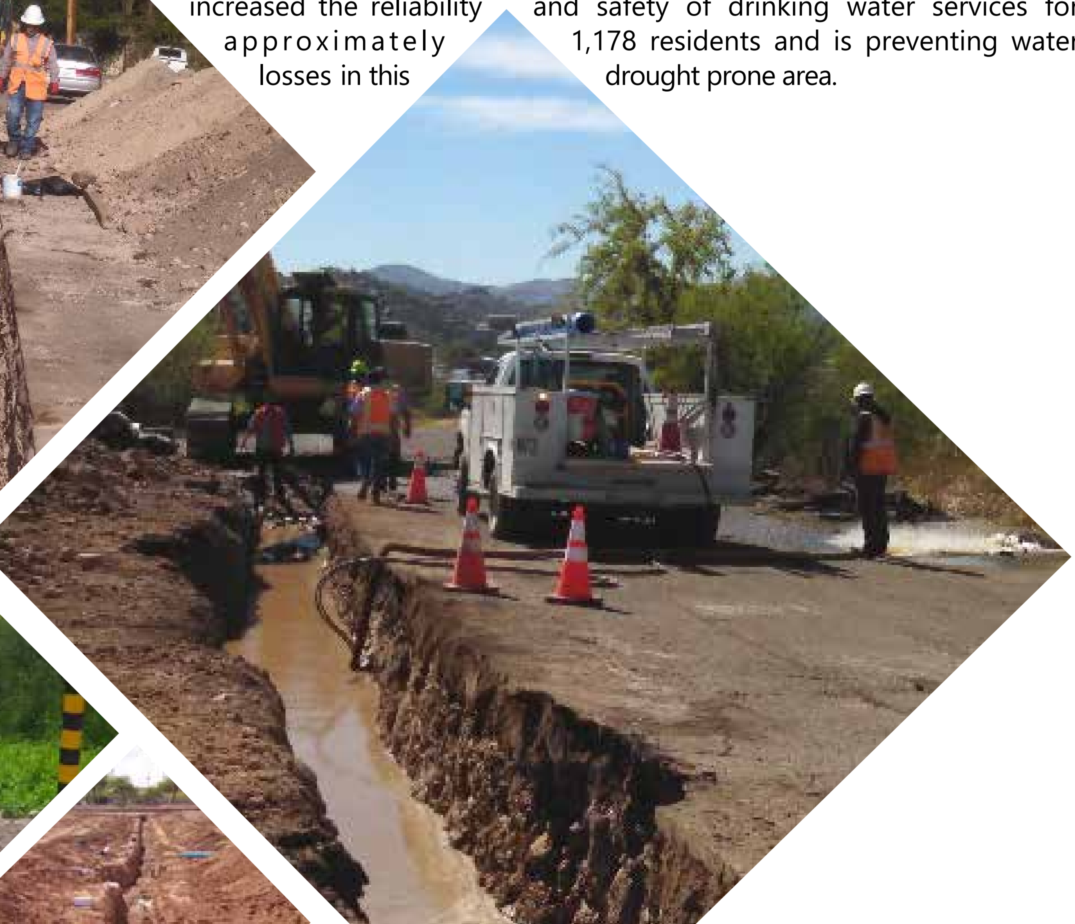
IMPROVING SERVICE

REDUCING WATER LOSSES

WATER MAIN REPLACEMENT ON CRAWFORD STREET
Nogales, Arizona
CAP Grant: US$500,000
Completed: August 2017

A new water distribution main was installed on Crawford Street, including the replacement of 50 water connections and meters, as well as seven fire hydrants. The old line, consisting of 4-inch cast iron pipe with lead fittings and 6-inch cement asbestos pipe, was built in 1918 and was experiencing frequent breaks, causing water losses, interrupting service and posing a potential risk for water quality and public safety issues. The new 8-inch polyvinyl chloride (PVC) waterline has increased the reliability and safety of drinking water services for approximately 1,178 residents and is preventing water losses in this drought prone area.

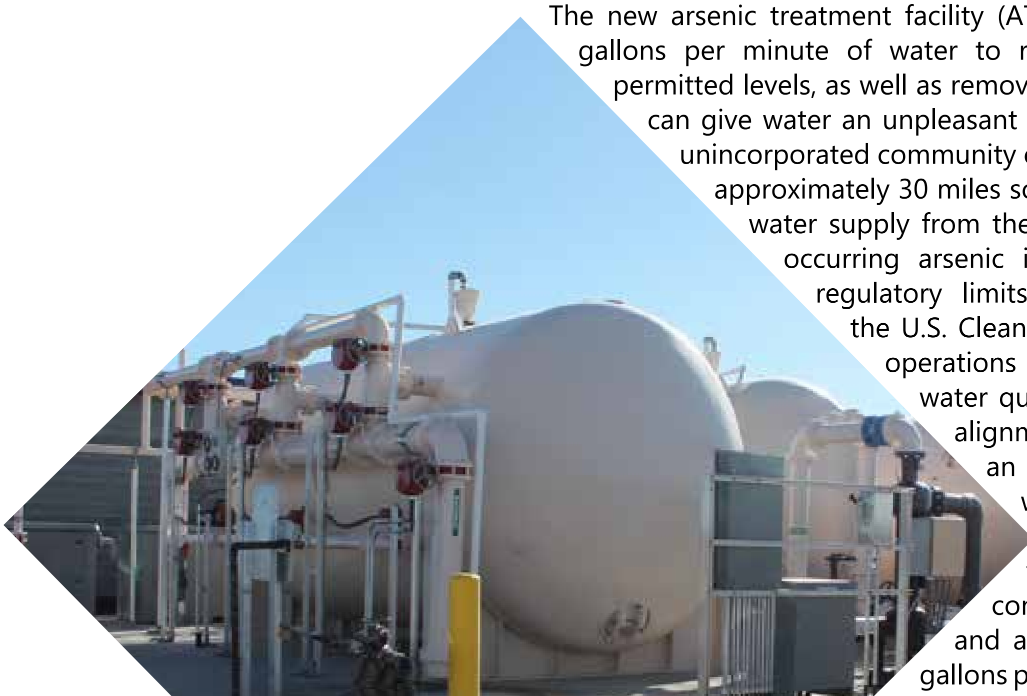




REDUCING
ARSENIC IN DRINKING WATER

ARSENIC TREATMENT AND WASTEWATER COLLECTION PROJECT
Tornillo, Texas
BEIF Grant: US$3.75 million
Completed: September 2017

The new arsenic treatment facility (ATF) has the capacity to treat 600 gallons per minute of water to reduce arsenic concentrations to permitted levels, as well as remove iron and manganese ions, which can give water an unpleasant taste, odor and color. Tornillo, an unincorporated community of about 3,500 residents, is located approximately 30 miles southeast of El Paso and obtains its water supply from the Hueco Bolson Aquifer. Naturally occurring arsenic in the aquifer regularly exceeds regulatory limits for potable water allowed by the U.S. Clean Water Act. The new plant began operations in February 2017, improving the water quality significantly. In addition, the alignment of the ATF waste line provided an opportunity to incorporate new wastewater connections, giving first-time access to sewer service to 19 households. The new sewer connections have all been installed and are collecting approximately 5,600 gallons per day of wastewater for treatment.



"Now that they put the filters, the difference is incredible! Now when you turn on the faucet, the water doesn't come out dark and brown like before. It's a huge difference."

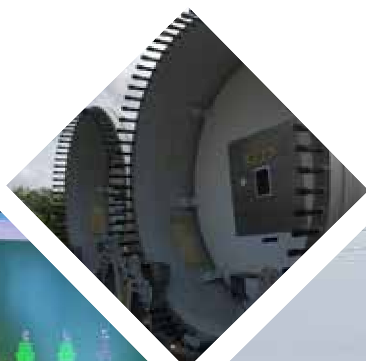
– **Saúl Erives**, a resident of Tornillo, Texas

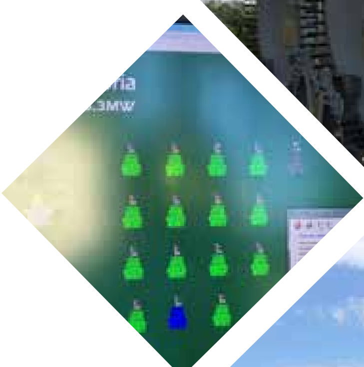
HARNESSING NATURE
TO GENERATE CLEAN ENERGY

417 MW OF NEW GENERATION CAPACITY INSTALLED
Loans: US$192.0 million

Project	Location	MW
EDPR Wind Energy Project	General Cepeda, COAH	199.5
Los Santos Solar I Project	Ahumada, CHIH	13.7
Rocksprings Wind Farm	Val Verde County, TX	149.3
SEPV Imperial Solar Project	Dixieland, CA	5.0
Victoria Wind Energy Project	Güémez, TAM	49.5
	Total	**417.0**

Five renewable energy projects funded with loans completed construction and began operation: three wind farms with a combined installed capacity of 398.3 megawatts (MW) located in Texas, Coahuila and Tamaulipas and two solar parks with a combined generation capacity of 18.7 MW located in California and Chihuahua. Altogether, these five plants are expected to produce 1.57 gigawatt-hours of clean electricity annually, sufficient to supply power to about 184,870 households. The power generated by these plants is helping improve air quality by preventing the emission of an estimated 805,400 metric tons of carbon dioxide and other greenhouse gases produced by conventional fossil fuel-based plants. All of these projects were co-financed by other financial institutions, with NADB providing 22.6% of the total financing.

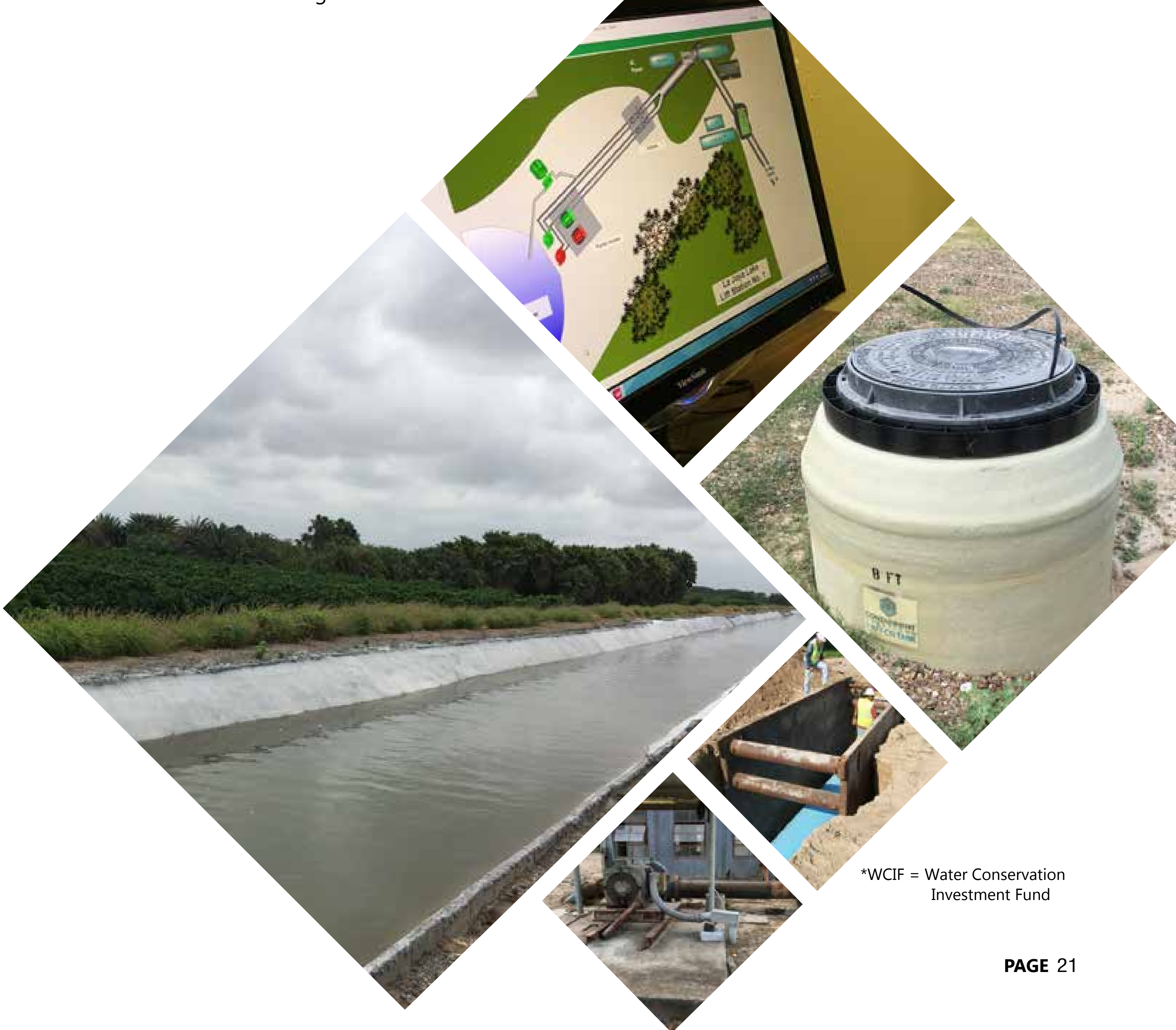




CONSERVING
ENERGY AND WATER FOR FARMERS

WATER CONSERVATION IMPROVEMENTS
Hidalgo County Irrigation District No. 16 In Texas
WCIF Grant: US$757,271
Completed: June 2017

Work to reline approximately 1.4 miles of the main canal was completed in June, the last component of a three-phase water conservation improvement project. The project also included construction of a 48-inch discharge line in Pump Station No. 1 at La Joya Lake, which was completed in January 2015, and installation of a flow control system completed in November 2016. The improvements have increased operational efficiency, reducing both energy consumption and water losses from seepage. The District is estimating annual water savings of around 746.8 million gallons and annual energy savings of 62,000 kilowatt-hours. In addition to benefitting district farmers and ranchers, the system also provides raw water to utilities serving local communities in the area.



*WCIF = Water Conservation Investment Fund

TECHNICAL ASSISTANCE
AND CAPACITY BUILDING

NADB provides grant support for project development, institutional strengthening and other initiatives through its Technical Assistance Program (TAP), as well as administers grants from the U.S. Environmental Protection Agency (EPA) through the Project Development Assistance Program (PDAP) and the U.S.-Mexico Border 2020 Program.

Highlights of the technical assistance activities carried out through all three programs during 2017 are summarized below, with the majority related to the water sector. More detailed information about each program is provided on the following pages.

2017 RESULTS

44 studies, capacity building and other development activities completed through the three programs funded by US$2.28 million in technical assistance grants and directly benefitting more than 45 communities in nine border states.

PROJECT DEVELOPMENT

FINAL DESIGNS	developed, reviewed or updated for 4 wastewater projects and 2 drinking water projects (TAP & PDAP)
ANALYSES OF ALTERNATIVES	to ascertain optimal project design and specifications for 2 wastewater projects and one binational storm drainage project (TAP & PDAP)
WATER AND/OR ENERGY AUDITS	aimed at improving operational efficiency of the water and wastewater systems for 3 U.S. and 2 Mexican communities (PDAP)
REGIONAL AND BINATIONAL PLANNING INITIATIVES	◆ Regional Water and Wastewater Service Plan for El Paso County, TX (TAP) ◆ Arizona-Sonora Environmental Strategic Plan 2017-2021 (TAP) ◆ Development Plan for the Rio Sonora Special Economic Zone (TAP)
ELECTRONIC-WASTE MANAGEMENT	benefitting 2 U.S. communities and 2 Mexican communities (B2020)

B2020 = U.S.-Mexico Border 2020 Program; PDAP = Project Development Assistance Program; TAP = Technical Assistance Program.

CAPACITY BUILDING

BASICS OF WATER UTILITY MANAGEMENT → 26 utility professionals from 11 Mexican communities earned diplomas from the Monterrey Technological Institute (ITESM) for completing the five-module (100-hour) course (UMI)

HAZMAT EMERGENCY RESPONSE TRAINING → through the creation of an institute for maquiladora workers in the Arizona-Sonora border region (B2020)

FAT, OIL AND GREASE PUBLIC OUTREACH CAMPAIGN → to improve operational efficiency of sewer systems in Brownsville, TX and Matamoros, TAM (B2020)

SECTOR STUDIES

PILOT SOLAR PLANT → for a children's cancer center, supplying more than 95% of the electricity needs of this non-profit medical facility and demonstrating the benefits of distributed generation (TAP)

PILOT TEST OF THE SUSTAINABLE COST MANUAL FOR MEXICAN WATER UTILITIES → developed by the Mexican National Water Commission and the Inter-American Development Bank (TAP)

B2020 = U.S.-Mexico Border 2020 Program; PDAP = Project Development Assistance Program; TAP = Technical Assistance Program;
UMI = NADB Utility Management Institute

TECHNICAL
ASSISTANCE PROGRAM (TAP)

Through this program, support is provided to border communities and project sponsors for the planning and development of projects, as well as for capacity-building initiatives, such as the seminars offered through the Utility Management Institute (UMI). Support may also be provided for studies to identify needs or generate knowledge about a new sector or technology.

During the year, a total of US$1.17 million in TAP grants was approved to fund 18 technical assistance projects, nine of which were completed prior to year-end. Among the activities approved was a state water plan for Chihuahua; emergency assistance to address transboundary sewer overflows in Naco, Sonora; and a preliminary engineering report and final design to repair a wastewater collector in Winterhaven, California.

TAP FUNDING APPROVED IN 2017
(US$)

Category	No. of Projects	Amount
Project development	7	$ 556,500
Capacity building	7	335,000
Sector studies	4	275,000
Total	**18**	**$ 1,166,500**

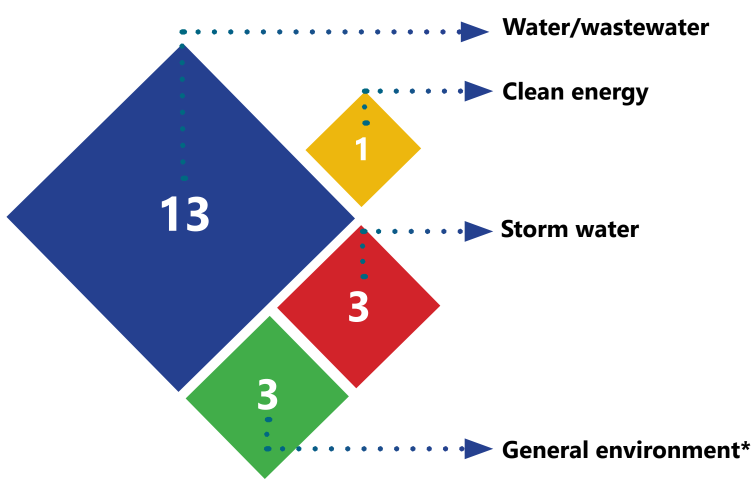
Twenty TAP projects were completed during the year, with US$834,765 in TAP grants. The majority of this assistance was directed toward the development of water-related infrastructure projects.

In addition to installing a pilot solar plant at a children's cancer center in Tijuana, Baja California, the two water system improvement projects in Altar and Trincheras, Sonora, which received TAP grants for final design activities, have already completed construction with funding from other sources.

Additionally, funding has been secured to implement four of the 15 priority projects identified in the Arizona-Sonora Environmental Strategic Plan 2017-2021. Two of those four projects were completed prior to year-end: establishing an ozone monitoring station in San Luis Rio Colorado, Sonora; and developing a mobile application to report daily air quality conditions in the Yuma-San Luis Rio Colorado region.

At the close of 2017, there were nine TAP-funded studies or other development activities in process.

SECTORS SUPPORTED IN 2017
(No. of projects)



* General environment includes activities related to more than one sector, such as state and binational planning initiatives.

TAP STUDIES COMPLETED IN 2017

	CATEGORY / LOCATION	SECTOR*	STUDIES	FUNDING (US$)
PROJECT DEVELOPMENT				
1	Altar, SON	W	Final design and procurement documents for a water transmission line	$ 8,954
2	Caborca, SON	WW	Final design for a wastewater collection project	30,080
3	Douglas, AZ and Agua Prieta, SON	SD	Evaluation of alternatives for flood mitigation	150,000
4	El Paso County, TX	W/WW	Regional Water and Wastewater Service Plan	86,832
5	La Joya, TX	WW	Final design for installation of residential sewer connections	50,000
6	Magdalena, SON	W	Water system sectorization study	44,004
7	Nogales, SON	WW	Meter placement study for International Outfall Interceptor	20,650
8	Sonora River watershed	GE	Development Plan for the Rio Sonora Special Economic Zone to help eight communities recover from a chemical spill in the river**	20,000
9	States of Arizona and Sonora	GE	Arizona-Sonora Environmental Strategic Plan 2017-2021	28,814
10	Trincheras, SON	W	Final design, geotechnical study and preparation of bid documents for a water supply project	5,750
CAPACITY BUILDING				
1-5	Hermosillo, SON	W/WW	Basics of Water Utility Management Modules I-V, benefitting 11 communities in Sonora	134,446
6	Piedras Negras, COAH	GE	Webinar, “Let’s Lower the Temperature: Climate Science in Action,” including a workshop for estimating greenhouse gas emissions related to implementing and operating water projects	5,833
SECTOR STUDIES				
1	Border-wide in Mexico	SD	Technical Guidelines for Designing Green Infrastructure Elements in Mexican Municipalities	44,358
2	Ciudad Juarez, CHIH; Nogales, SON; and Tijuana, B.C.	SD	Recommendations for amending municipal regulations to incorporate low-impact development concepts in urban infrastructure	40,044
3	Piedras Negras, COAH	W/WW	Pilot test of sustainable costs manual for water utilities in Mexico	40,000
4	Tijuana, B.C.	ENE	Pilot solar plant for a children’s cancer center	125,000
20			**TOTAL**	**$ 834,764**

* ENE = Clean energy; SD = Storm drainage; W = Drinking water; WW = Wastewater; GE = General environment, which includes activities related to more than one sector.
** Includes the communities of Bacoachi, Banámichi, Huépac, Ures, Baviácora, San Felipe de Jesús, Aconchi and Arizpe.

PROJECT DEVELOPMENT
ASSISTANCE PROGRAM (PDAP)

Through this EPA-funded program, support is provided for studies and other activities related to the development and design of water and wastewater projects that have been prioritized to receive a construction grant through the Border Environment Infrastructure Fund (BEIF), as well as to reinforce the long-term sustainability and proper operation of those projects.

During 2017, EPA approved US$1.03 million in grants to fund 18 studies to support the development of 15 water and wastewater projects located on both sides of the border. Eleven PDAP studies were also completed, supporting the development of nine infrastructure projects. Two of those projects were approved to receive BEIF financing prior to year-end: Rehabilitation of the Collector Poniente in Tijuana, Baja California, and the Wastewater Infrastructure Project in Marathon, Texas.

PDAP FUNDING APPROVED IN 2017
(US$)

Location	No. of Studies	Amount
Mexico	8	$ 209,702
United States	10	819,838
Total	**18**	**$ 1,029,540**

At the close of 2017, there were 14 PDAP-funded studies in process.

PDAP STUDIES COMPLETED IN 2017

	LOCATION	SECTOR*	STUDIES	FUNDING (US$)
MEXICO				
1	Camargo, TAM	WW	Update of final design for wastewater collection and treatment project	$ 81,411
2	Diaz Ordaz, TAM	WW	Wasteload evaluation of the water quality of the Rio Grande at the discharge point of the Diaz Ordaz WWTP and transboundary environmental information document	48,121
3	Diaz Ordaz, TAM	WW	Water and energy audits of the water and wastewater system	33,579
4	Nueva Ciudad Guerrero, TAM	WW	Water and energy audits of the water and wastewater system	21,652
5	Tecate, B.C.	WW	Analysis of alternatives for a wastewater collection and treatment project in Ejido Nueva Colonia Hindú	27,242
6	Tijuana, B.C.	WW	Analysis of alternatives for replacing part of the Poniente Collector	28,166
7	Tijuana, B.C.	WW	Mexican environmental impact document for the Poniente Collector	12,519
UNITED STATES				
1	El Paso County, TX	WW	Final design of the Cuadrilla WWTP	414,389
2	Marathon, TX	WW	Water audit of the water and wastewater system	64,218
3	Presidio, TX	W	Energy audit of the water and wastewater system	31,731
4	Sunland Park, NM	WW	A water audit, water conservation and rate study for Camino Real Regional Utility Authority (CRRUA)	107,326
11			**TOTAL**	**$ 870,354**

W = Drinking water; WW = Wastewater; WWTP = Wastewater treatment plant.

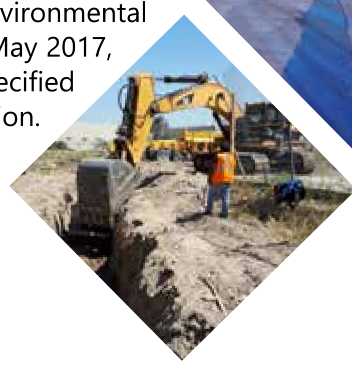
The following studies illustrate the support provided to project sponsors through PDAP.

TIJUANA, BAJA CALIFORNIA

ANALYSIS OF ALTERNATIVES AND ENVIRONMENTAL IMPACT DOCUMENT FOR SEWER IMPROVEMENTS

Two studies were carried out to support the development of a project to replace deteriorated sections of the sewer line, Poniente Collector, which runs parallel to the Tijuana River. Having determined that using the same alignment as the current pipeline would entail right-of-way and technical issues that could affect the successful implementation of the project, the local water utility, CESPT, requested assistance in evaluating various technical options for pipe alignment of section 1-A of the collector. The evaluation took into consideration the proposed layout of related sub-collectors, topography and soil conditions, constructability criteria, right-of-way and easement requirements, construction and operation costs, and compliance with applicable standards, among other factors. The results of the analysis indicated that the most viable option was the modified design proposed by CESPT, which was subsequently reviewed and validated by the Mexican National Water Commission.

The second study provided support in preparing the environmental impact statement, which was required to obtain state authorization to build the project. The document identifies the potential environmental impacts of building and operating an infrastructure project and indicates any measures to be taken by the project sponsor to mitigate those impacts. The statement concluded that replacing the Poniente Collector is necessary to eliminate wastewater spills and reduce human health risks and that the potential environmental impacts would mainly be intermittent, temporary and insignificant. Based on this document, the Baja California Ministry of Environmental Protection authorized the project in May 2017, subject to implementation of the specified mitigation measures during construction.



MARATHON, TEXAS

WATER AUDIT OF THE WATER AND WASTEWATER SYSTEM

To support the long-term sustainability of the water and wastewater system, a water audit was performed to identify potential problems in the distribution system and improve the utility's revenue streams and operational efficiency. Real losses from the water system were found to be within the normal parameters for a utility the size of Marathon. However, the audit did identify issues with some of the production and commercial meters. The faulty commercial meters have been replaced, ensuring that the utility accurately charges users for the volume consumed. As part of the water audit, a rate study was also performed, and recommendations were made that could improve revenue streams.

U.S.-MEXICO
BORDER 2020 PROGRAM

Border 2020 is a binational program developed by EPA and the Mexican Ministry of Environment and Natural Resources (SEMARNAT) to improve the environment and protect the health of residents within 100 kilometers of both sides of the border. The program focuses on five key goals related to clean air, access to safe drinking water, waste management, joint emergency preparedness and environmental stewardship. NADB administers funds from EPA, providing logistical and administrative services with respect to identifying, contracting and managing projects and workshops funded under the program.

Thirteen initiatives were completed during the year, including four waste management projects, mainly related to recycling and final disposal of electronic waste, and three related to storm water management techniques. In addition, a permanent HAZMAT training institute for maquiladora workers was established at the *Tecnológico de Nogales* (ITN) in Nogales, Sonora, with support from Arizona State University (ASU) in Nogales, Arizona. These 13 initiatives represent a total investment of US$937,669, with Border 2020 covering 63% of the cost.

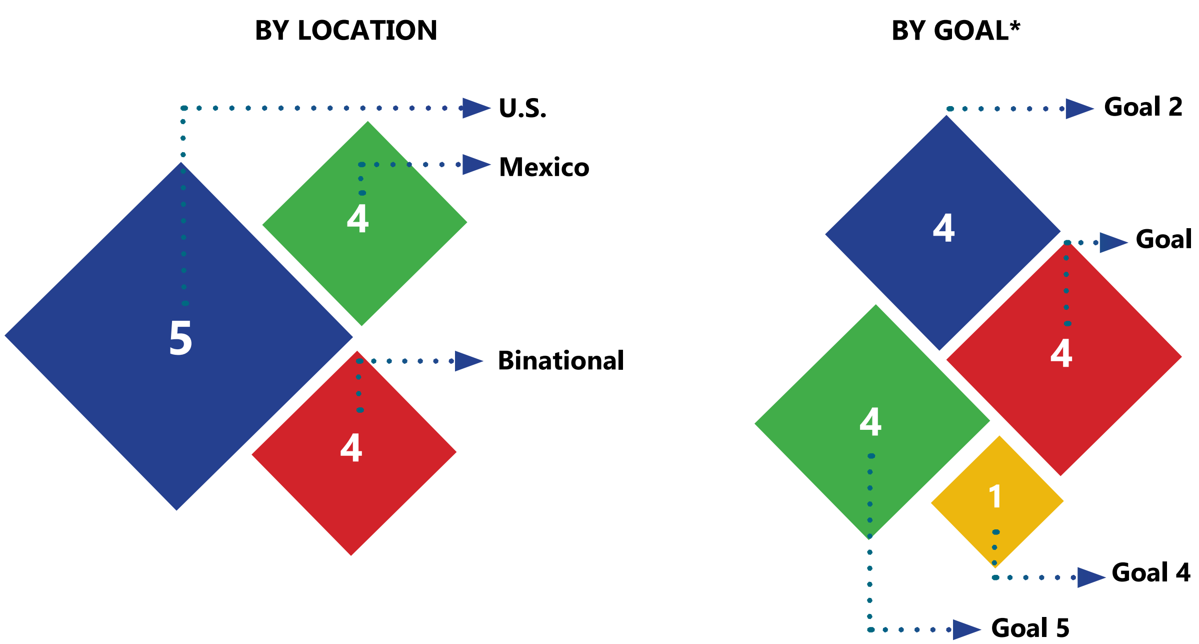
Following a request for proposals in mid-2017, EPA authorized approximately US$1.42 million in grant funding for 25 projects to be implemented beginning in 2018: 14 projects totaling US$612,572 in Region 6 and 11 projects totaling US$805,000 in Region 9.

BORDER 2020 STUDIES COMPLETED IN 2017
(US$)

Location	No. of Studies	Amount
Region 6*	6	$ 411,148
Region 9**	7	177,670
Total	**13**	**$ 588,818**

* Region 6 covers New Mexico, Texas, Chihuahua, Coahuila, Nuevo Leon and Tamaulipas.
** Region 9 covers Arizona, California, Baja California and Sonora.

BORDER 2020 STUDIES COMPLETED IN 2017
(No. of projects)



* Goals: 1. Reduce air pollution; 2. Improve access to clean and safe water; 3. Promote material management, waste management and clean sites; 4. Enhance joint preparedness for environmental response; 5 Compliance assurance and environmental stewardship.
No project related to Goal 1 was completed in 2017.

BORDER 2020 STUDIES COMPLETED IN 2017

	GOAL / COMMUNITY	SECTOR*	STUDY	FUNDS (US$)
GOAL 2: IMPROVE ACCESS TO CLEAN AND SAFE WATER				
1	Brownsville, TX	WW	Fat, Oil and Grease (FOG) Public Outreach Campaign aimed at raising awareness regarding the proper disposal of these materials to improve the operational efficiency of the sewer system	$25,000
2	Ciudad Juarez, CHIH	SD	Demonstration project using low-impact development techniques to create passive rainwater harvesting systems in a community park	43,204
3	Edinburg, TX	SD	Determining the ideal bioswale porous material for storm water management in South Texas	26,022
4	Nogales, SON	SD	Community outreach presentations, intensive design training and collaborative demonstration projects to strengthen local capacity in the use of green infrastructure techniques to control erosion and sediments in creeks	53,927
GOAL 3: PROMOTE MATERIAL MANAGEMENT, WASTE MANAGEMENT AND CLEAN SITES				
1	Nogales, SON	SW	Pilot electronic-waste management program for chemical laboratories	20,894
2	Pharr, TX	SW	Programs to raise public awareness regarding the proper disposal of e-waste, recyclable materials and used tires to reduce illegal dumping	36,390
3	Piedras Negras, COAH and Eagle Pass, TX	SW	Comprehensive binational e-waste recycling program aimed at waste reduction and pollution prevention in local landfills	36,054
4	Tijuana, B.C.	SW	Pilot program for separation of municipal solid waste by source at the residential suburb level and using the organic waste for composting	73,483
GOAL 4: ENHANCE JOINT PREPAREDNESS FOR ENVIRONMENTAL RESPONSE				
1	Arizona and Sonora border region	HW	A sustainable HAZMAT Emergency Response Training Institute for maquiladora workers	79,611
GOAL 5: COMPLIANCE ASSURANCE AND ENVIRONMENTAL STEWARDSHIP				
1	Arizona and Sonora border region	GE	Evaluation of the state of environmental health along the Arizona-Sonora border	37,975
2	Border wide	GE	Border 2020 Program Indicator Reports	45,000
3	Nuevo Laredo, TAM	GE	Law reform and environmental education to improve implementation of environmental legislation, strengthen environmental cooperation and the exchange of information with Laredo, TX, and train environmental inspectors and staff	11,000
4	El Centro, Calexico and Brawley, CA	GE	Environmental health and asthma awareness campaign in low-income housing communities of Imperial County	100,258
13			**TOTAL**	**$ 588,818**

GE = General environment; HW = Hazardous waste; SD = Storm drainage; SW = Solid waste; WW = Wastewater

COLLABORATIVE INITIATIVES
AND FUNDING PARTNERSHIPS

In carrying out its mandate, NADB and BECC have pursued partnerships with other public and private organizations in an effort to promote environmental projects on the border and identify additional support for their development and implementation. Several long-standing and successful partnerships have been established with federal and state agencies, financial and academic institutions and private-sector organizations in both countries, whose support has been instrumental in helping NADB carry out its mission in benefit of the border communities. Some of the collaborative initiatives carried out or ongoing in 2017 are highlighted below.

- PILOT TEST OF THE SUSTAINABLE COST MANUAL FOR MEXICAN WATER UTILITIES, funded with the Inter-American Development Bank (IDB) and developed in collaboration with the Mexican National Water Commission (CONAGUA) and the local water utility in Piedras Negras, Coahuila. The methodology outlined in the manual was applied on a test basis to the utility, with immediate results, including improved commercial efficiency and cost savings.

- PILOT SOLAR PLANT FOR A CHILDREN'S CANCER CENTER IN TIJUANA, B.C., implemented in collaboration with the Castro-Limón Foundation and Mission Solar Energy, a photovoltaic solar panel manufacturer based in San Antonio, Texas, which donated the solar panels. The solar plant is supplying up to 95% of the electricity needs of the Centro Oncológico Pediátrico (COP) de Tijuana, established by the Castro-Limón Foundation to provide comprehensive medical care free of charge to children with cancer who have no other medical support.

- BORDER LOW-IMPACT DEVELOPMENT INFRASTRUCTURE FORUM IV: RESILIENCE AND COMPETITIVENESS FOR U.S.-MEXICO BORDER CITIES. Hosted by BECC, in collaboration with the Government of the State of Sonora and the Commission on Environment and Sustainable Development (CEDES), the forum highlighted case studies where low-impact development techniques have been successfully used on both a micro and macro regional level and the importance of updating local regulations to guarantee their implementation, among other topics.

- LINE OF CREDIT FOR DEVELOPMENT OF WATER AND WASTEWATER PROJECTS IN MEXICO, with the German development bank, Kreditanstalt für Wiederaufbau (KfW), which was used in 2017 by NADB to fund part of the loans for the desalinization plant in Ensenada, Baja California, and the cogeneration facility for the South Wastewater Treatment Plant in Ciudad Juárez, Chihuahua.

- ENERGY EFFICIENCY LEARNING NETWORK FOR WATER UTILITIES IN COAHUILA, in partnership with the non-profit German corporation, Deutsche Gesellschaft für Internationale Zusammenarbeit GmbH, México (GIZ), and the Coahuila State Water and Wastewater Commission. Since 2015, fourteen utilities have been participating in diverse training and project development activities supported by technical assistance.

- SUSTAINABLE E-WASTE MANAGEMENT AND RECYCLING SYSTEM IN MEXICALI, B.C., funded and developed with BECC, the IDB Multilateral Investment Fund (MIF), the Massachusetts Institute of Technology (M.I.T.), SEMARNAT, EPA, the Baja California Ministry of Environmental Protection and the Universidad Autónoma de Baja California (UABC). This three-year project to establish a safe and efficient recycling program for used electronic devices will be completed in 2018.

MEASURING
PROJECT SUCCESS

To measure the impact of projects, NADB and BECC have established a results measurement process consisting of two components: a closeout report completed after the project has been in operation for a year; and an impact assessment for selected projects. The closeout report verifies whether the project was constructed as approved and has been operating as intended, while the impact assessment is performed to ascertain the actual impact of the project on specific environmental and human health indicators.

PROJECT CLOSEOUT
RESULTS

During 2017, the Bank completed 28 closeout reports: 12 for loan projects, 12 for BEIF-funded projects, and four for CAP-funded projects.

As of December 31, 2017, closeout reports have been completed for 76 projects, representing a total investment of US$1.4 billion and benefitting 9.2 million border residents.

To illustrate project impact, the closeout results for projects in the water and clean energy sectors are highlighted on the next page.

CLOSEOUT REPORTS COMPLETED BY SECTOR
AS OF DECEMBER 31, 2017

Sector	No. of Reports	Final Cost (US$ Million)	Population Benefitted*
Air quality	4	$ 166	5,600
Basic urban infrastructure	2	44	25,654
Clean energy	8	498	3,538,998
Public transportation	2	43	3,500,000
Solid waste	8	18	2,292,549
Water and wastewater	51	638	3,359,290
Water conservation	1	1	1,155
Total	**76**	**$ 1,408**	**9,223,246**

* Population figures do not duplicate benefitted residents in communities with more than one project. The population for public transportation is not included in the total population, as those communities were already counted in other projects.

DRINKING WATER SECTOR

7 PROJECTS

resulting in the construction of four water treatment plants with a total installed capacity of 21.5 million gallons a day (mgd) and 113 miles of pipeline, which are benefitting 61,920 border residents.

INDICATOR	ACTUAL	% ACHIEVED*
Increased access to water service (mgd)	20.5	100%
Improved water quality (mgd)	1.5	100%
Residential water hookups (number of homes)	13,414	91%
Total investment cost (US$ millions)	$52.2	

* Percentage achieved compared to the outcomes expected at certification.

WASTEWATER SECTOR

42 PROJECTS

resulting in the construction, expansion or rehabilitation of 24 wastewater treatment plants with a total installed capacity of 231 million gallons a day (mgd), 706 miles of pipeline and 27 lift stations, which are benefiting 3.3 million border residents.

INDICATOR	ACTUAL	% ACHIEVED*
Increased access to wastewater service (mgd)	227	94%
Reduced discharges of untreated wastewater (mgd)	173	74%
Residential sewer connections (number of homes)	319,035	80%
Total investment cost (US$ millions)	$500	

* Percentage achieved compared to the outcomes expected at certification.

CLEAN ENERGY SECTOR

8 RENEWABLE ENERGY PROJECTS

consisting of 4 solar parks and 3 wind farms with a total installed capacity of 514 megawatts and a biodiesel production plant, which altogether are benefiting 3.5 million border residents.

INDICATOR*	ACTUAL	% ACHIEVED**
Power generation (gigawatt-hours/year)	1,456	91%
Biodiesel production (gallons a year)	11,000,000	45%
Greenhouse gas emissions prevented ($MTCO_2eq$/yr.)	855,287	83%
Other emissions prevented (MT/yr. of NOx, SO_2)	2,127	93%
Total investment cost (US$ millions)	$497.6	

* $MTCO_2eq$/yr. = Metric tons of carbon dioxide equivalent /year; SO_2 = Sulfur dioxide; NOx = Nitrogen oxides
** Percentage achieved compared to the outcomes expected at certification.

ASSESSING
PROJECT IMPACT

During 2017, a third impact assessment was completed for a wastewater project benefiting two communities in the Lower Valley region of El Paso County, Texas—the first to be performed on a project in the United States. The results of this study are described below.

For the next impact assessment, NADB plans to develop a study aimed at documenting the results of wastewater infrastructure projects in a binational context. Unlike previous assessments that only considered the impact on the community directly benefitted, this study will evaluate how infrastructure improvements in one city have impacted the adjacent city on the other side of the border. After exploring several options, the sister cities of Nogales, Arizona and Nogales, Sonora were selected for the study, which is expected to be completed in early 2019.

IMPACTS OF WATER AND WASTEWATER
GO BEYOND THE ENVIRONMENT
EL PASO, TEXAS

In March 2017, a third impact assessment was completed, which evaluated the overall health and quality of life of the communities of Socorro and San Elizario in the Lower Valley region of El Paso, Texas, following a US$98-million water and wastewater project completed in 2003. Financing for the project was provided by EPA through the Border Environment Infrastructure Fund (BEIF), by the Texas Water Development Board (TWDB) through its Economically Distressed Areas Program (EDAP), and by the U.S. Department of Agriculture Rural Development (USDA-RD), among other sources, including equity investments made by the project sponsor, Lower Valley Water District (LVWD).

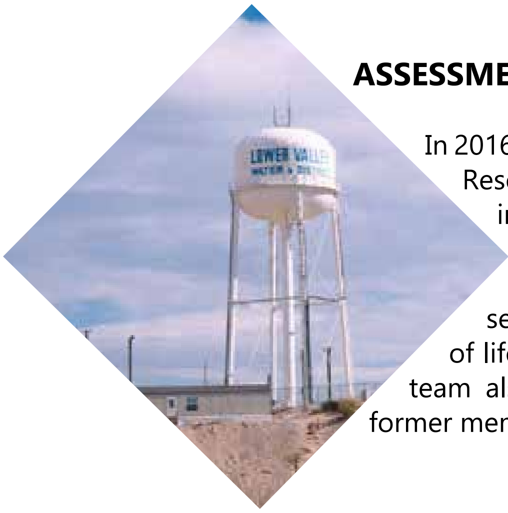
WATER AND WASTEWATER PROJECT FOR THE LOWER VALLEY WATER DISTRICT

SPONSOR:	Lower Valley Water District (LVWD)
CERTIFIED:	June 24, 1998
COMPLETED:	May 19, 2003
POP. BENEFITTING	70,000
COST:	US$98.35 million
DESCRIPTION:	

Construction of a three-phase water and wastewater project. Phase I completed prior to certification included extension of waterlines to six subdivisions in Socorro and the installation of master water meters. Phase II included construction of wastewater mains and lift stations, as well as a large water transmission line and storage facilities, among other improvements. Phase III covered construction of wastewater mains and lift stations, as well as water transmission mains, a booster station and reservoir. Sewer and water distribution lines in several subdivisions in Socorro and San Elizario were also installed, including residential hookups.

BACKGROUND

Prior to the installation of the water distribution and sewer systems, residents of Socorro and San Elizario relied solely on trucked, well and bottled water for their drinking water supply and used septic tanks and cesspools for wastewater disposal. The inadequate design and construction of these on-site disposal systems resulted in contamination of residential wells. In the early 1990s, the El Paso County Health Department reported high rates of Hepatitis A and shigella dysentery in the area. In addition, a study by the University of Texas at San Antonio Health Science Center found that 90% of San Elizario residents sampled had been infected with Hepatitis A before reaching the age of 35. Less serious health issues caused by water contamination included skin problems, gastrointestinal illnesses and stomach infections.

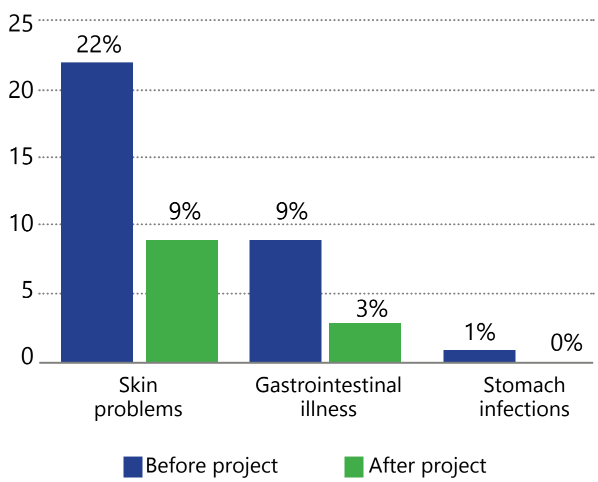


ASSESSMENT

In 2016, a team consisting of staff from BECC, LVWD, and the Center for Environmental Research Management (CERM) at the University of Texas at El Paso (UTEP), gathered information through surveys, interviews and secondary data. They surveyed the residents of 100 households who had lived in the same home for over 25 years. The questionnaire covered such topics as water and wastewater services before and after the project, changes in health conditions and quality of life, and economic growth and development since project implementation. The team also conducted formal interviews with government officials, utility staff and former members of the project steering committee established for the EDAP funding.

SURVEY RESULTS

PERCENTAGE OF RESIDENTS SURVEYED REPORTING HEALTH ISSUES



COMMENTS FROM RESPONDENTS

"...we used to struggle to bathe, brush our teeth...without water we are nothing."

"Huge difference. We don't have to bother neighbors for water even though we would pay for it. I used to shower with a bowl to pour water."

"By having water, we have a bathroom. Now we just open the faucet. Before I had to warm the water... Without water we can't live. Water is life..."

RESULTS

The overall impact of the new water and wastewater systems has been overwhelmingly positive. One hundred percent of residents in San Elizario and Socorro now have running water and 93% of households are connected to the sewer system. These infrastructure improvements have not only improved daily living conditions, they have also significantly reduced health problems. As reported by residents in the survey, the incidence of skin problems was reduced from 22% to 9% and gastrointestinal disease from 9% to 3%.

Having access to water and sewer services has also spurred economic and community development. Between 2000 and 2015, medium household income increased between 12% and 28%, while between 2000 and 2010 property values increased 41% in Socorro and 23% in San Elizario. Residents have noticed the positive change in the community, as 93% of those surveyed believe the water and sewer systems have benefitted the community through the growth of local businesses, increased parks and recreation, improved fire safety and expanded healthcare services.

NADB CUMULATIVE RESULTS
1995-2017

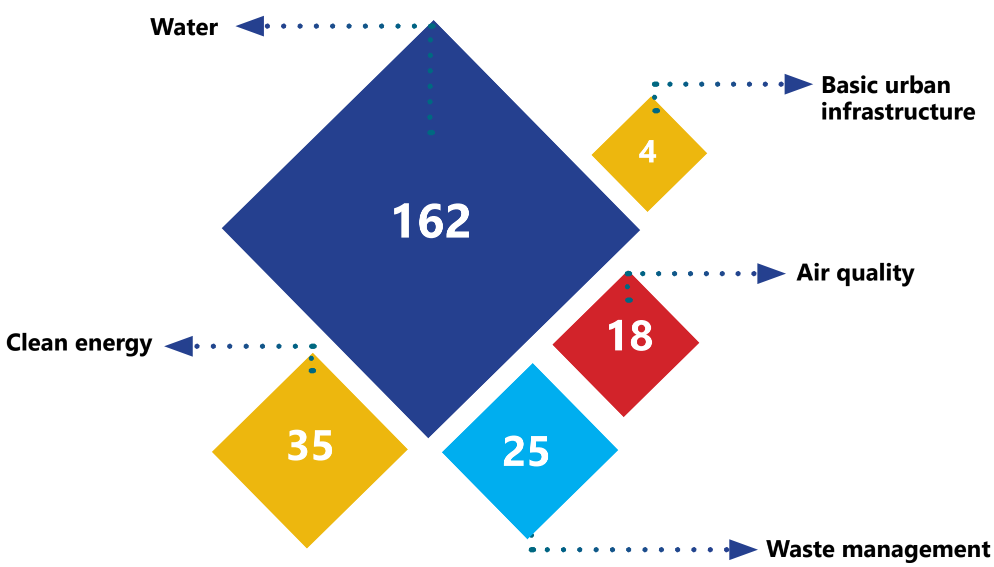
With its own resources, leveraged borrowings and grants from the U.S Environmental Protection Agency (EPA), NADB is transforming border communities with sustainable infrastructure, benefitting more than 17 million residents in the U.S.-Mexico border region.

As of December 31, 2017, NADB had contracted more than US$3.0 billion to support the implementation of 244 environmental infrastructure projects. Of those funds, US$2.25 billion was in the form of loans and US$94.8 million in grants. The remaining $658.7 million was provided by EPA and used by NADB to finance water and wastewater projects through the Border Environment Infrastructure Fund (BEIF).

PROJECT FINANCING BY STATE 1995-2017

State	Population Benefitted	Total Projects	Financing Contracted
UNITED STATES			
Arizona	142,121	21	$ 204.66
California	1,686,358	25	413.10
New Mexico	178,061	11	40.21
Texas	1,469,389	55	604.42
Border region		1	25.00
Subtotal U.S.	**3,475,929**	**113**	**$ 1,287.39**
MEXICO			
Baja California	2,840,000	29	$ 376.00
Chihuahua	1,898,778	30	181.32
Coahuila	1,063,231	10	146.67
Nuevo Leon	4,586,048	11	273.72
Sonora	1,310,183	28	215.90
Tamaulipas	2,117,804	21	484.42
Border Region		2	39.55
Subtotal Mexico	**13,816,044**	**131**	**$ 1,717.58**
TOTAL	**17,086,882**	**244**	**$ 3,004.97**

PROJECTS FINANCED BY SECTOR 1995-2017



SECTION 2
FINANCIAL REPORT

MANAGEMENT
DISCUSSION & ANALYSIS

FINANCIAL HIGHLIGHTS

NADB continued its successful record of financing infrastructure in the border region that helps preserve, protect and enhance the environment while operating in a strong and financially sound manner. As detailed in this report, 10 new projects were approved with financing totaling US$288.4 million for their implementation, while US$113.9 million in loans and grants were disbursed for the execution of 30 projects, with more than half of those projects in the water and wastewater sector. Moreover, 11 projects were completed, including a cogeneration facility with the capacity to supply part of the electricity to operate a wastewater treatment plant in Ciudad Juarez, Chihuahua, and improvements to an irrigation system that is preventing an estimated 747 million gallons a year of water losses from seepage and spillage for farmers in Hidalgo County, Texas.

In the area of technical assistance and institutional strengthening, US$1.17 million in grants were approved through the Technical Assistance Program (TAP) to fund 18 studies, training seminars and other development activities. Prior to the institutional merger, BECC also administered US$1.36 million in grants approved by the U.S. Environmental Protection Agency (EPA): US$1.03 million through the Project Development Assistance Program (PDAP) and US$334,615 through the U.S.-Mexico Border 2020 Program. As part of its ongoing technical assistance strategy, NADB will continue to pursue partnerships with other entities aimed at creating synergies that support the development of environmentally sustainable and resilient border communities.

NADB set a goal for the maintenance of its high credit rating (Moody's Aa1 and Fitch AA) as a strategic priority. With this measure, the levels of activity in lending and the projected financial ratio goals were set. In 2017, NADB maintained its loan portfolio balance relatively flat, yet it resulted in the highest net income in its history. This strategy is especially important as the Bank is in the process of increasing its capital stock, a process that can take some time.

Beginning the year with a loan balance of US$1.4 billion, the Bank disbursed US$101.43 million on contracted loans and was repaid US$218.92 million on amortizing loans. The net effect of loans disbursed versus amortizing payments would have represented a slight growth of less than 0.23%. However, the prepayment of loans in 2017 was unusually high with a total of US$120.80 million, representing 8.6% of the total portfolio. The prepayments included the largest loan in the portfolio and reflect changing conditions in the renewable energy sector as consolidation and maturation of the industry occurs. The repayments are viewed as favorable to NADB operations, as they provide liquidity for the Bank and the opportunity for additional lending in sectors in need of development bank assistance.

The Bank is in the process of requesting additional capital from its two shareholder governments and is aware that this process may take time. It is with this reality in mind that NADB has established the abovementioned strategy. It is the Bank's intention to maintain this strategy at the level of its current ratios.

In July 2017, NADB funded the first repayment of its outstanding bonds. The US$300 million in bonds issued in October 2013 will mature in October 2018, and the funding of this cash requirement was done in compliance with the Bank's liquidity policy. The next bond maturity will be in February 2020 in the amount of US$250 million and as such will require the funding of this amount in October 2018.

A concise look at the major sectorial components of operations on a historical basis is summarized in Tables 1 and 2.

TABLE 1:
FINANCIAL SUMMARY 2013-2017[1]
(US$ Thousands)

	2017	2016	2015	2014	2013
BALANCE SHEET DATA					
Cash and investments	**$ 954,962**	$ 511,558	$ 504,861	$ 442,954	$ 545,525
Loans outstanding[2]	**1,293,807**	1,411,296	1,324,777	1,185,514	1,011,212
Total assets	**2,145,753**	1,812,866	1,780,599	1,633,369	1,573,076
Borrowings outstanding, gross	**1,493,443**	1,187,505	1,190,550	1,059,953	1,046,386
Total liabilities	**1,511,438**	1,208,832	1,215,017	1,090,683	1,054,422
Total equity	**634,315**	604,034	565,582	542,686	518,654
Callable capital	**2,351,667**	2,351,667	2,295,000	2,295,000	2,295,000
INCOME STATEMENT DATA					
Total interest income	**$ 68,622**	$ 59,012	$ 51,246	$ 43,710	$ 39,543
Loans	**57,761**	52,427	45,892	38,487	35,149
Investments	**10,861**	6,585	5,354	5,224	4,394
Interest expense	**31,640**	19,950	15,101	13,548	10,838
Net interest income	**36,982**	39,061	36,145	30,163	28,705
Total operating expenses	**8,448**	17,934	18,143	10,816	19,451
Provision for loan losses	**(3,945)**	5,134	8,559	2,199	10,544
Total non-interest income (expense)	**3,156**	(369)	2,388	(1,093)	(888)
Income before program activity	**31,690**	20,758	20,389	18,254	8,366
Net program expenses[3]	**2,163**	1,088	4,873	2,077	1,145
Net income	**29,527**	19,670	15,516	16,177	7,221
RATIOS					
Total equity / loans outstanding	**49.0%**	42.8%	42.7%	45.8%	51.3%
Gross debt / callable capital	**63.5%**	50.5%	51.9%	46.2%	45.6%
Gross debt / total equity	**235.4%**	196.6%	210.5%	195.3%	201.8%
Interest coverage[4]	**1.8x**	2.3x	2.8x	2.6x	2.8x
Liquid assets / total assets	**44.3%**	25.3%	25.3%	23.8%	31.3%
Income before program activity / total equity	**5.0%**	3.4%	3.6%	3.4%	1.6%
Income before program activity / average assets	**1.6%**	1.2%	1.2%	1.1%	0.6%
CREDIT RATINGS					
Moody's Investor Service	**Aa1/P-1**	Aa1/P-1	Aa1/P-1	Aa1/P-1	Aaa/P-1
Fitch Ratings	**AA/F1+**	AA/F1+	AA/F1+	AA/F1+	AA/F1+

[1] Excludes the U.S. domestic program (see Note 8 of the consolidated financial statements).

[2] Before allowance for loan losses, unamortized fees, and effect of foreign exchange adjustments and hedged items.

[3] Program expenses include grant financing and technical assistance funded from the Bank's retained earnings.

[4] Interest coverage ratio is defined as interest income minus operating expenses less provision for loan losses divided by interest expense.

TABLE 2:
PROJECT AND FINANCING OPERATIONS 2013-2017

(US$ Thousands)

	2017	2016	2015	2014	2013
PROJECT CERTIFICATION					
Total projects certified[1]	**10**	15	14	16	19
By sector					
Water	**5**	7	7	10	8
Waste management	**-**	5	-	-	-
Air quality[2]	**-**	1	1	1	1
Basic urban infrastructure[3]	**-**	-	1	1	1
Clean and efficient energy	**5**	2	5	4	9
By financing type					
Loans	**6**	3	8	7	11
NADB-funded grants	**-**	7	2	2	5
NADB-administered grants	**4**	5	4	7	3
LENDING OPERATIONS					
Loans approvals	**$ 283,233**	$ 96,876	$ 239,177	$ 323,670	$ 273,242
Loan commitments	**229,536**	146,767	178,262	304,323	349,881
Loan disbursements	**101,426**	136,253	249,556	254,163	214,964
Principal payments	**218,915**	49,734	110,297	76,122	73,733
Loan prepayments	**120,795**	6,632	53,584	1,136	12,362
GRANT OPERATIONS					
NADB-funded grants[4]					
Approved	**$ -**	$ 3,100	$ 1,000	$ 765	$ 2,183
Contracted	**1,500**	1,600	1,450	315	2,183
Disbursed[5]	**1,178**	550	3,694	1,318	455
NADB-administered grants[6]					
Approved	**6,236**	25,022	20,274	24,936	6,104
Contracted	**14,535**	21,231	16,219	12,047	7,658
Disbursed	**11,278**	10,228	8,698	14,673	17,459

[1] Project certification and financing proposals are approved simultaneously by the Board of Directors.
[2] This category includes street paving, other roadway improvements, industrial emissions reduction and public transportation.
[3] These projects consist of works from various sectors, such as roadway improvements, water and sewer lines, storm drainage, and public lighting.
[4] Grants funded from designated retained earnings of the Bank for certified infrastructure projects (excludes technical assistance).
[5] Includes grant disbursements for project implementation and expenditures for project supervision for 2014-2017.
[6] Grants funded by EPA and administered by NADB through the Border Environment Infrastructure Fund (BEIF).

PROJECT AND FINANCING OPERATIONS

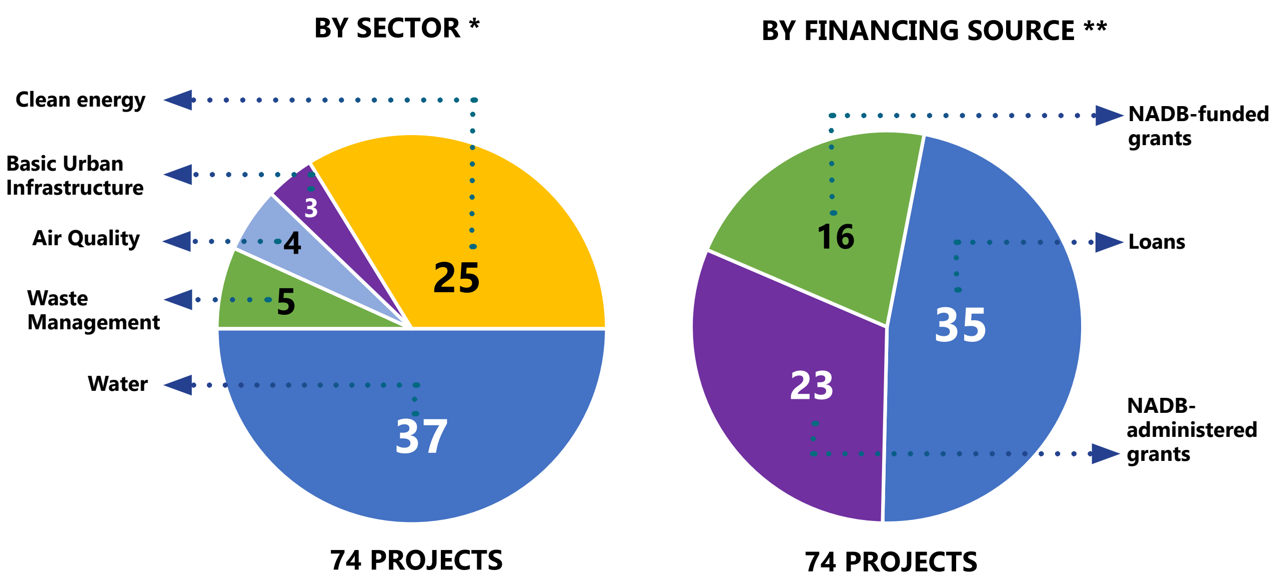
PROJECT CERTIFICATION

NADB continued to advance its environmental mandate on the border by developing and submitting certification and financing proposals to its Board of Directors for approval. During 2017, the Board certified 10 projects, including five clean energy projects representing a total of 780 megawatts of new generation capacity from renewable sources and five wastewater system improvement projects that will collect and/or convey an estimated 7.6 million gallons a day of sewage to treatment plants. During the previous year, 15 projects were certified, including a second public transportation project for the purchase of low-emission buses in Mexico and a Property-Assessed Clean Energy (PACE) funding program to support energy efficiency, renewable energy and water conservation improvements in non-residential properties in the United States.

A breakdown of the number of projects certified by environmental sector and financing type over the past five years is provided in Table 2. From 2013-2017, the Board certified a total of 74 projects, representing an average of 15 projects a year. During that period, half of the certified projects were in the water sector and close to half were financed with loans (Figure 1).

While water-related projects will remain a priority for the institution, the Bank is continually exploring other opportunities for addressing critical environmental issues along the border.

FIGURE 1:
BREAKDOWN OF CERTIFIED PROJECTS (2013-2017)



* Water includes drinking water, wastewater, storm water and water conservation. Air quality includes roadway improvements, public transportation and reduction of industrial emissions. Basic urban infrastructure are projects that consist of a mix of works from various sectors, such as street paving, water and sewer lines, storm drainage and public lighting.

**NADB-administered grants are funded by EPA through the Border Environment Infrastructure Fund (BEIF).

LENDING ACTIVITY

NADB continues to pursue a lending strategy based on prudent capital and risk management. Following a surge in lending activity fueled by its entry into the renewable energy sector at the beginning of the decade, NADB is now taking a smaller stake in large projects, not only as a means of reducing its credit risk exposure and managing its capital resources, but also to encourage increased investment from the private sector in public infrastructure and services. As a result, the approval and disbursement of new loans has leveled off over the past five years with loan approvals averaging US$243.24 million a year and disbursements averaging US$191.27 million a year (Table 2).

During 2017, new loans totaling US$283.23 million were approved for six projects; loan agreements totaling US$229.54 million were signed with the sponsors of seven projects, including five of the loans approved during the year; and US$101.43 million was disbursed to support the implementation of 11 projects, including additional disbursements under the revolving credit lines for two low-emission bus programs. In contrast, during 2016, the Bank approved US$96.88 million in loans for four projects; contracted four loans for US$146.77 million and disbursed US$136.25 million to support the execution of seven projects.

A breakdown of lending activity by environmental sector for the past two years is presented in Table 3. The majority of loan disbursements in 2017 were channeled to wind farms (72.0%), followed by solar parks (10.9%) and water-related projects (10.8%). The remainder went to public transportation (4.9%) and basic urban infrastructure (1.4%), which consists of a mix of works such as street paving, water and sewer lines, storm drainage and public lighting. In comparison, wind energy accounted for 76.3% of disbursements in 2016, followed by public transportation (21.5%), with the remaining balance going to solar and other clean energy (2.2%).

Private-sector borrowers in the U.S. accounted for 35.5% of the disbursed loans in 2017, while the remaining 64.5% went to projects in Mexico and was divided among public (2.8%), private 52.3%) and public-private borrowers (9.4%). In comparison, all the loans disbursed in 2016 went to projects located in Mexico, with the majority going to private-sector borrowers (99.3%) and the remainder to public-private partnerships (0.7%).

Principal payments totaled US$218.91 million in 2017, including the prepayment of three loans totaling US$120.79 million and the liquidation of a short-term loan for US$32.69 million. In comparison, the Bank received US$49.73 million in principal payments in 2016, including the prepayment of one loan totaling US$6.63 million. Principal payments, excluding prepayments, have averaged US$66.86 million annually over the past five years (Table 2).

TABLE 3:
LENDING ACTIVITY BY SECTOR IN 2016 AND 2017

(US$ Millions)

PROJECT TYPE	APPROVALS		SIGNINGS		DISBURSEMENTS	
	2017	**2016**	**2017**	**2016**	**2017**	**2016**
Air quality	**$ -**	$ -	**$ -**	$ 18.00	**$ -**	$ -
Basic urban infrastructure*	**-**	-	**-**	-	**1.39**	-
Energy efficiency	**-**	50.00	**25.00**	-	**-**	-
Other clean energy	**-**	-	**-**	-	**-**	0.97
Public transportation	**-**	26.25	**-**	26.25	**4.97**	29.36
Solar energy	**105.50**	11.00	**67.75**	-	**11.08**	2.02
Water / wastewater	**10.05**	9.63	**-**	9.63	**10.97**	-
Wind energy	**167.68**	-	**136.79**	92.89	**73.02**	103.90
Total	**$ 283.23**	$ 96.88	**$ 229.54**	$ 146.77	**$ 101.43**	$ 136.25

* These projects consist of a mix of works from various sectors, such as street paving, water and sewer lines, storm drainage and public lighting.

Table 4 provides a summary of lending activity during the past two years and its impact on the loan portfolio.

TABLE 4:
SUMMARY OF ANNUAL LENDING ACTIVITY AND BALANCES
(US$ Millions)

	12/31/2017	12/31/2016
Outstanding balance, beginning of year*	**$ 1,411.30**	$ 1,324.78
Loan disbursements	**101.43**	136.25
Principal repayments	**(218.91)**	(49.73)
Loans written off	**-**	-
Outstanding balance, end of year*	**$ 1,293.81**	$ 1,411.30
Loans contracted, pending disbursement	**$ 188.35**	$ 58.52
Loans approved, pending contracting	**136.14**	159.19
Total loan commitments	**324.49**	217.71
Outstanding loans & loan commitments	**$ 1,618.30**	$ 1,629.01

* Outstanding balances, before allowance for loan losses, unamortized fees, and effect of foreign exchange adjustments and hedged items.

LOAN PORTFOLIO

NADB closed the year with an outstanding loan balance of US$1.29 billion, a decrease of 8.3% compared to the balance at the end of 2016 (US$1.41 billion). This decrease is in line with the Bank's more moderate lending strategy and also reflects the prepayment of two loans totaling US$113.22 million in the last quarter of the year. Nevertheless, since December 31, 2013, the loan portfolio has grown at an average annual rate of 6.4% (Figure 2).

While the loan balance declined slightly in 2017, the number of projects per sector with loans outstanding remained relatively stable, with the majority in the water and wastewater sector (Figure 3). In general terms, water-related projects represented 47.4% of the portfolio in 2017, down slightly from 50.6% in 2016 due to the liquidation of three loans, including the only water conservation loan. Clean and efficient energy projects increased from 31.6% to 35.9% by year-end, as loans for new projects outpaced the liquidation of loans for prior projects, while air quality improvement projects remained fairly stable at 16.7%, compared to 17.7% at the beginning of the year.

FIGURE 2:
ANNUAL LOAN PORTFOLIO PERFORMANCE

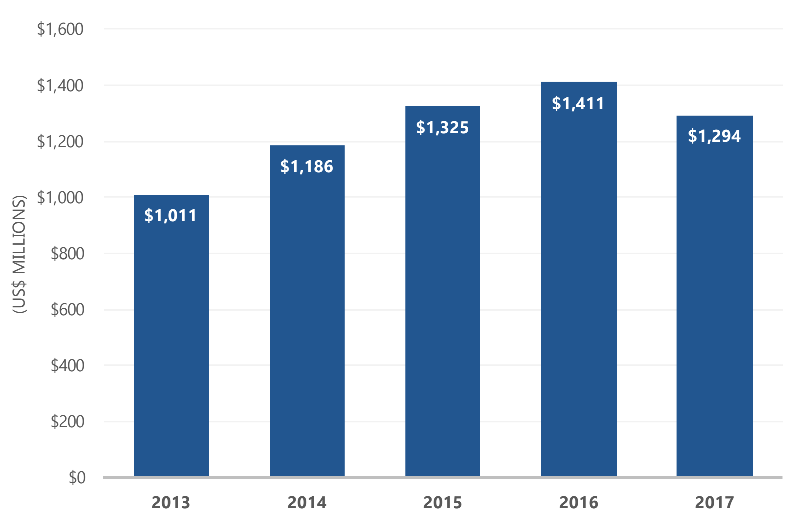
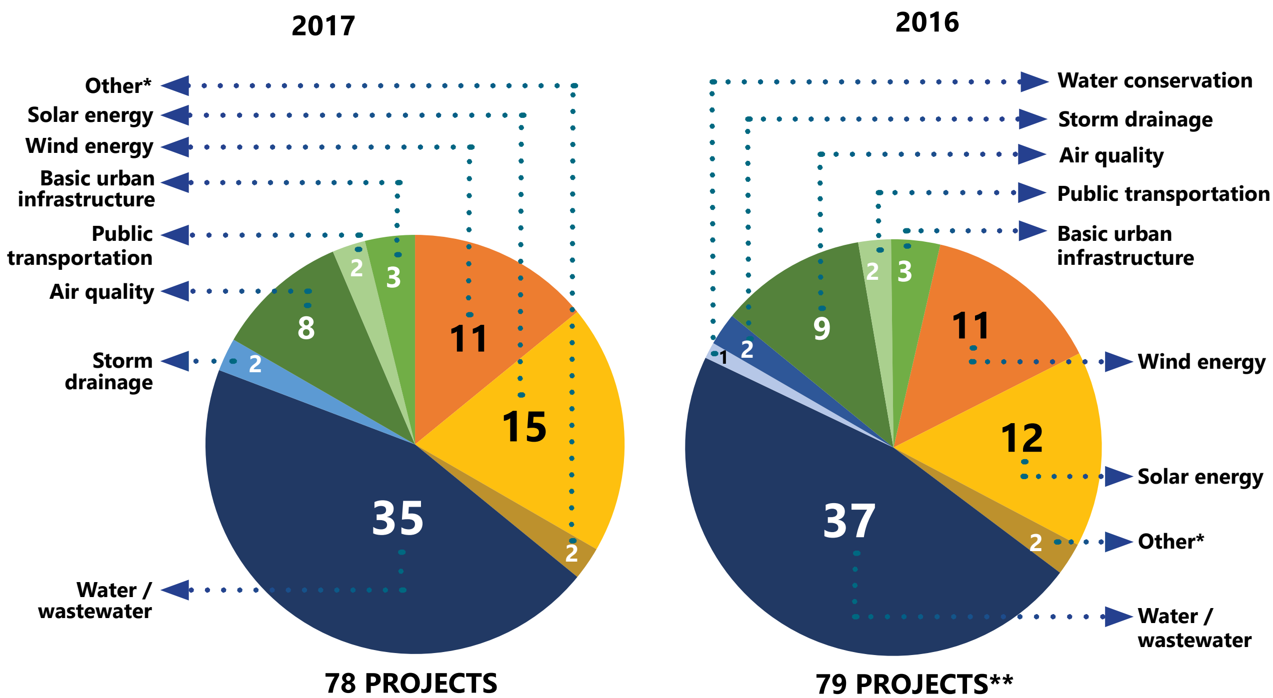


FIGURE 3:
BREAKDOWN OF LOAN PORTFOLIO BY NUMBER OF PROJECTS



* Other includes cogeneration and landfill gas-to-energy projects.
** 2016 project figures were adjusted to include three wastewater projects partially funded by a loan, which were omitted from the last report.

As previously indicated, principal payments outstripped disbursements practically across the board in 2017, shrinking the outstanding balance in every sector category except basic urban infrastructure (Table 5). Wind energy registered the largest decline (US$86.55 million), which was mainly attributable to the prepayment of a loan for US$101.20 million, followed by water and wastewater with a decrease of US$11.06 million, mainly due to the prepayment of a loan for US$12.02 million. However, the most significant change was due to the prepayment of the only water conservation loan (US$7.39 million), thereby eliminating that category.

Since the decline in the outstanding balance was spread across almost all categories and the number of categories was reduced, there was relatively little effect on year-end portfolio distribution by sector (Figure 4). At the close of 2017 and 2016, wind energy accounted for the largest portion of the loan portfolio at 48.0% and 50.1%, respectively; followed by solar energy with 22.5% and 20.7%, respectively; while water and wastewater remained stable at 12.4% and 12.2%, respectively.

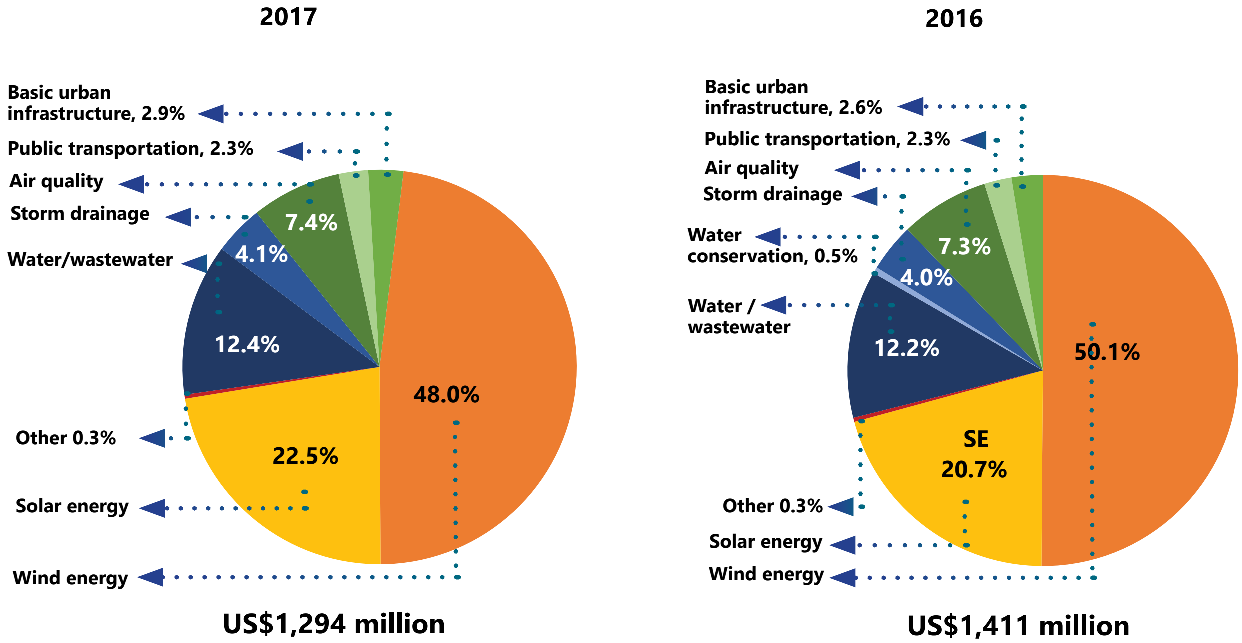
Given that the border region offers ideal conditions for solar and wind energy projects and that the Mexican

TABLE 5:
PORTFOLIO EVOLUTION BY ENVIRONMENTAL SECTOR
(US$ Millions)

	12/31/2017	12/31/2016	CHANGE (%)
Wind energy	**$ 620.67**	$ 707.22	-12.2
Solar energy	**291.20**	291.53	-0.1
Water/wastewater	**161.08**	172.14	-6.4
Air quality	**95.63**	103.69	-7.8
Storm drainage	**52.72**	56.25	-6.3
Basic urban infrastructure*	**37.09**	36.38	2.0
Public transportation	**31.16**	31.87	-2.2
Water conservation	**–**	7.39	-100.0
Other clean energy**	**4.26**	4.83	-11.8
Total	**$ 1,293.81**	$ 1,411.30	

* Basic urban infrastructure includes a mix of street paving, water and sewer lines, storm drainage and public lighting.
** Other clean energy includes cogeneration and landfill gas-to-energy projects.

FIGURE 4:
DISTRIBUTION OF THE OUTSTANDING BALANCE BY ENVIRONMENTAL SECTOR



Other includes cogeneration and landfill gas-to-energy projects

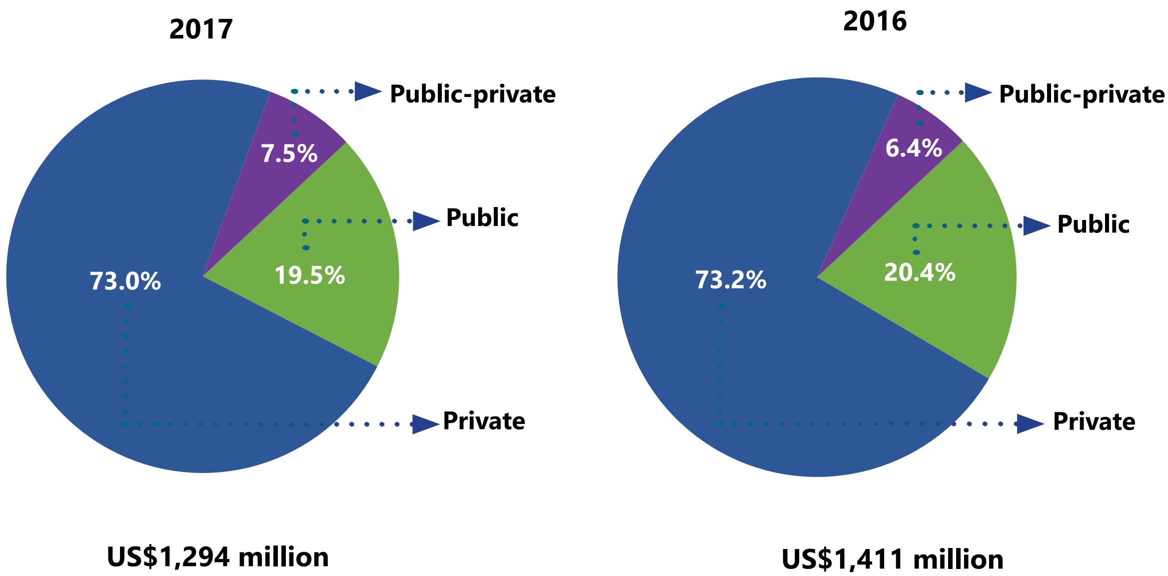
renewable energy market is just taking off under the recent power industry legislation, the Bank expects to see continued demand for loans in those sectors. Demand for water and wastewater projects is also expected to remain steady as local governments work to replace aging systems or extend these vital services to unserved areas.

In terms of borrowers, the loan portfolio is divided into three categories: public, private or public-private. In the latter case, a private company is the direct borrower, but the source of payment and/or guaranty is a public utility or local government and the Bank has recourse to both the private and public entity. Figure 5 shows the distribution of the loan portfolio by borrower type at the close of 2016 and 2017.

In 2017, because of changing economic conditions, a higher than usual number of borrowers prepaid their loans. Consequently, following six years of steady growth, outstanding loans held by private sector borrowers decreased US$87.96 million to US$944.80 million during 2017, largely due to the prepayment of the wind loan (US$101.20 million). During the same period, outstanding loans held by governmental borrowers decreased US$35.75 million to US$252.56 million, in part due to the prepayment of two loans totaling US$19.59 million. Loans held by public-private borrowers increased slightly from US$90.23 million to US$96.45 million.

The downward trend in public sector lending is expected to continue as state and local governments constrained by budgetary and legal restrictions are increasingly looking to public-private partnerships to provide public services and infrastructure. Private sector lending, on the other hand, is expected to revert to its previous pattern of steady growth given the high demand and interest of private investors in the emerging renewable energy market in Mexico. Of the US$188.35 million in loan commitments pending disbursement at the end of 2017, 96.5% (US$181.75 million) is destined for private sector borrowers with projects related to renewable energy, public transportation and the reduction of industrial emissions.

FIGURE 5:
DISTRIBUTION OF THE OUTSTANDING BALANCE BY BORROWER TYPE



Public-private borrower generally refers to a loan structure in which a private company is the borrower, but the source of payment and/or guaranty is a public utility or local government.

In terms of portfolio distribution by geographic region, growth continued along the same lines as the previous year albeit at varying rates. Loans invested in Mexican projects grew by US$22.80 million (2.9%) to a total of US$815.59 million at the close of 2017, compared to an increase of US$114.61 million (16.9%) in 2016. The amount held by U.S. borrowers decreased US$140.28 million (22.7%) to a total of US$478.21 million, following a decline of US$28.09 million (4.3%) the previous year. The accelerated decline in U.S. loans can be attributed in part to the prepayment of two loans totaling US$113.22 million. In addition, although two loans totaling US$35.99 million were disbursed for projects in the United States during 2017, one was a short-term loan that was fully repaid prior to year-end (US$32.69 million).

As a result, at the close of 2017, 63.0% of the balance of outstanding loans were held by borrowers with projects in Mexico and the remaining 37.0% were related to projects in the United States (Figure 6). Nevertheless, of the US$188.35 million in loan commitments pending disbursement at the close of 2017, approximately 17.4% (US$32.69 million) is destined for U.S. projects.

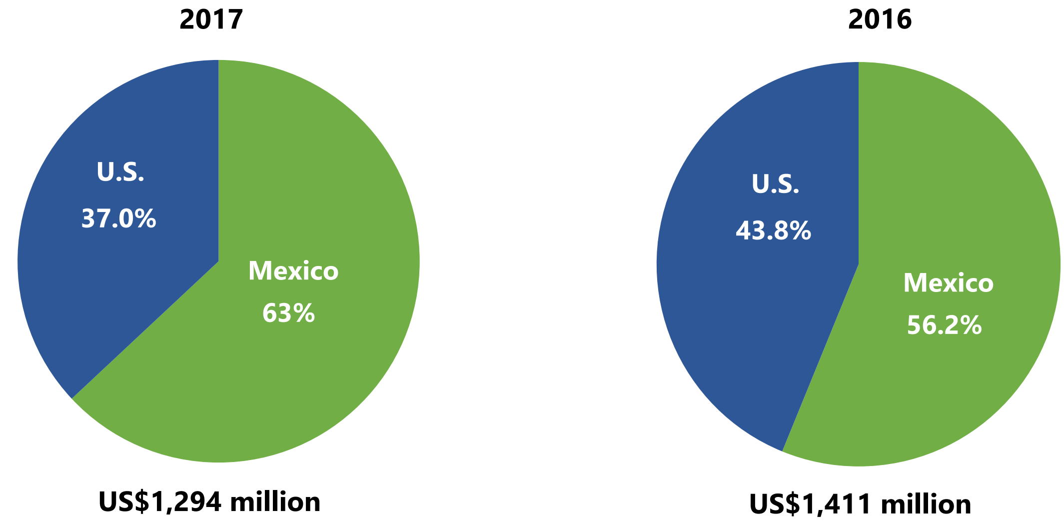
Changes in the balance of outstanding loans by state during the 12-month period ending December 31, 2017, are provided in Table 6. Lending activity in 2017 was spread across eight of the ten border states within the geographic jurisdiction of the Bank, with the largest disbursements made to projects in

TABLE 6:
PORTFOLIO EVOLUTION BY STATE*
(US$ Millions)

	12/31/2017	12/31/2016	Change (%)
Texas	**$ 269.45**	$ 303.82	-11.3
Tamaulipas	**265.74**	276.40	-3.9
Nuevo Leon	**174.69**	160.82	8.6
California	**136.29**	238.80	-42.9
Baja California	**109.71**	103.99	5.5
Coahuila	**93.08**	78.47	18.6
Sonora	**88.03**	86.26	2.1
Arizona	**72.48**	75.88	-4.5
Chihuahua	**53.18**	54.99	-3.3
Mexican border**	**31.16**	31.87	-2.2
Total	**$ 1,293.81**	$ 1,411.30	

* Includes loans to both public and private borrowers.
** Border-wide program, with current participants from Baja California, Chihuahua, Nuevo Leon and Sonora.

FIGURE 6:
DISTRIBUTION OF THE OUTSTANDING BALANCE BY COUNTRY



Texas (US$32.69 million), Nuevo Leon (US$24.56 million) and Coahuila (US$15.77 million). On the other hand, principal payments outstripped disbursements in six states, with the largest payments made in California (US$105.82 million), followed by Texas (US$67.06 million), which included the liquidation of the US$32.69 million short-term loan disbursed during the year.

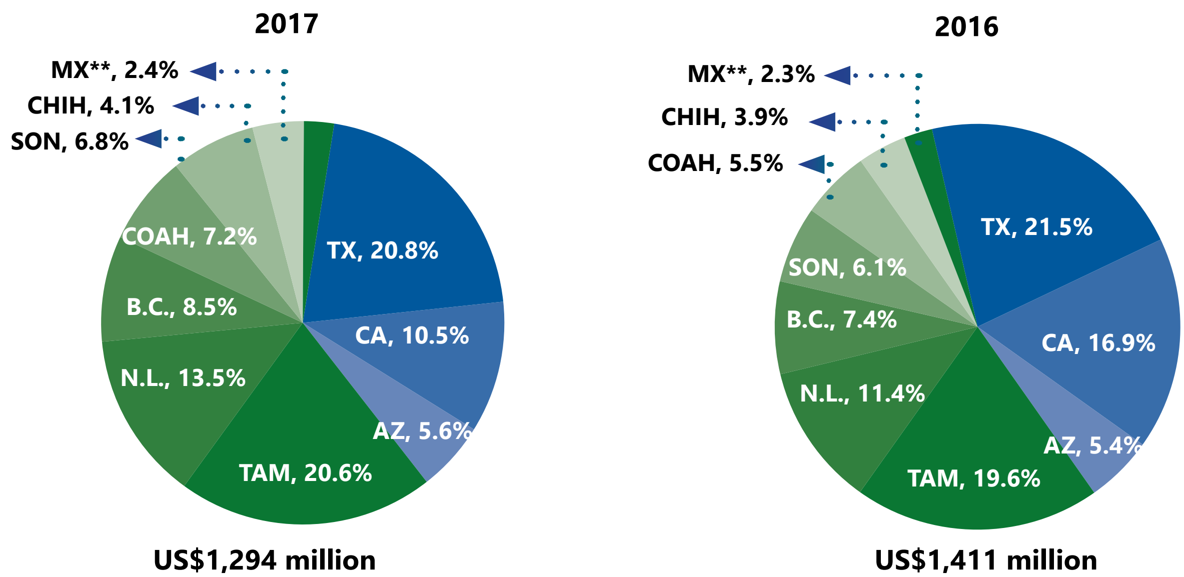
As a result of this lending activity, the portfolio was not only more evenly distributed among the states by year-end, there was also a shift in the states with the largest loan concentrations (Figure 7). At the beginning of the year more than half (58.0%) of the portfolio was concentrated in the states of Texas (21.5%), Tamaulipas (19.6%) and California (16.9%), but by year-end Nuevo Leon had displaced California and the overall level of concentration of the top three states had dropped to 54.9%, with Texas accounting for 20.8% of the loan portfolio, followed by Tamaulipas (20.6%) and Nuevo Leon (13.5%). Moreover, the combined participation of the three states with the smallest share of the portfolio continued to grow, from 14.8% at the beginning of the year to 16.5% by year-end. New Mexico is the only eligible state with no outstanding loan.

Non-performing Loans. Of the 71 loans outstanding at the close of 2017, one was classified as non-performing with a balance of US$14.38 million, representing 1.1% of the loan portfolio. However, after several delays in construction, the project began operation in July 2017. No loan was classified as non-performing at the close of 2016. The Bank classifies loans as non-performing when payments of principal or interest on the loan are delinquent for 90 days or more, or where reasonable doubt exists as to the borrower's ability to make timely payment.

In the event that the full repayment of a loan is deemed doubtful, the Bank allocates a specific allowance for probable and estimable loan losses on its financial statements. As of December 31, 2017 and 2016, the Bank had a specific allowance for loan losses of US$2.67 million and US$0, respectively. The Bank also provides a general allowance for loan losses for all outstanding loans based on statistical cumulative default and recovery rates for project finance loans. As of December 31, 2017 and 2016, the general allowance totaled US$18.44 million and US$25.05 million, respectively.

Lending Limits. Under the charter, the total amount of outstanding loans (and guaranties) may not at any time exceed the total amount of unimpaired subscribed capital of the Bank, plus the unimpaired reserves and undistributed surplus that are included in its capital resources. As of December 31, 2017, the total unimpaired

FIGURE 7:
LOAN PORTFOLIO DISTRIBUTION BY STATE*



* Includes loans to both public and private borrowers.
** Border-wide program, with current participants from Baja California, Chihuahua, Nuevo Leon and Sonora.

subscribed capital of the Bank was just under US$2.77 billion (paid-in capital and corresponding callable capital) and its unimpaired reserves and undesignated retained earnings came to US$194.02 million, for a total loan limit of US$2.96 billion, an increase of US$34.42 million (1.2%) over the loan limit of US$2.93 billion at the end of 2016. At the close of 2017, the balance of outstanding loans (US$1.29 billion) represented 43.7% of this limit.

The Bank also imposes limits per project and per borrower. By policy, NADB cannot lend a project more than 85% of eligible project costs. Since 2013, the single obligor limit (SOL) is set at 20% of the sum of funded, unimpaired paid-in capital, plus undesignated retained earnings, the Special Reserve, and the Capital Preservation Reserve. An additional 10% may be made available for obligors that meet certain risk-related criteria. At the close of 2017, the SOL was US$101.25 million, 3.9% higher than that of 2016 (Table 7).

Nevertheless, as explained previously, the Bank has been pursuing a more moderate lending strategy by taking smaller stakes in large projects. The largest loan contracted in 2017 was for US$74.10 million, and the largest loan outstanding at year-end had a balance of US$89.25 million.

TABLE 7:
SINGLE OBLIGOR LIMITS (SOL)
(US$ Millions)

	12/31/2017	12/31/2016	Change
20% SOL	**$ 110.27**	$ 106.09	$ 4.18
30% SOL	**165.40**	159.13	6.27

GRANT ACTIVITY

NADB-funded Grants. With the approval of the Board of Directors, NADB may use a portion of its retained earnings to finance critical environmental infrastructure projects in low-income communities with grants through the Community Assistance Program (CAP).

During 2017, the Bank signed grant agreements totaling US$1.50 million for three projects approved in 2016 and disbursed US$979,685 in CAP grants to support the implementation of five projects. A summary of annual financing activity through CAP for the past two years, as well as the overall status of the program at the end of 2017, is presented in Table 8.

As part of its funds management strategy for 2017, the Bank set an annual disbursement budget of US$2.00 million for this program. Since nine previously approved projects with grants totaling US$4.1 million were entering the implementation phase at the beginning of the year, no new projects were submitted for approval during 2017. For 2018, the Bank has raised the disbursement cap to U$3.00 million, which will provide an opportunity for the approval of new projects. Since program inception in 2013, grant approvals have averaged US$1.41 million a year, while grant disbursements have averaged US$647,694 annually.

A small portion of CAP funding is used to cover the supervision costs of the projects financed under the program. A cumulative total of US$731,652 was committed to supervision contracts as of December 31, 2017, representing 5.2% of the funding allocated to the program. For the years ended December 31, 2017 and 2016, US$198,527 and US$112,812, respectively, were expended under supervision contracts.

For 2017, the Board approved the allocation of an additional US$2.00 million in retained earnings for this program. Additionally, in accordance with Board Resolution 2013-16, which terminated the Water Conservation Investment Fund (WCIF), US$619,425 in unused WCIF grant funds were rolled over to the CAP program prior to year-end. As of December 31, 2017, NADB had a balance of US$6.75 million in uncommitted CAP funding available for future projects.

TABLE 8:
COMMUNITY ASSISTANCE PROGRAM
ANNUAL FINANCING ACTIVITY AND PROGRAM STATUS

(US$ Millions)

	2017	2016	Cumulative
Retained earnings allocated	**$ 2.62**	$ -	$ 14.09
Funds allocated for supervision	**0.22**	0.12	0.73
Grants approved[1]	**-**	3.10	6.61
Grants contracted[1]	**1.50**	1.60	6.61
Grants disbursed[2]	**0.98**	0.32	3.24
Cancellations[3]	**(0.17)**	-	(0.43)
Contracted grants, not yet disbursed			$ 3.38
Approved grants, not yet contracted			-
Funding available for future projects[4]			6.75

[1] Annual and cumulative figures, less unused funds deobligated from completed projects.
[2] Excludes disbursements for supervision.
[3] Unused funds deobligated from completed CAP projects and returned to the CAP program for future projects.
[4] Allocated retained earnings less approved grants and funds allocated for supervision.

Administered Grants. NADB administers grant funds provided by EPA through the Border Environment Infrastructure Fund (BEIF) for the implementation of priority water and wastewater projects. These funds are received from EPA prior to disbursement by the Bank to the grantees, and any BEIF-related operating expenses incurred by the Bank are reimbursed by EPA. Consequently, these funds are reflected in the consolidated financial statements, but have no economic effect on its operations.

During 2017, BEIF grants totaling US$6.24 million were approved for six projects, including additional funding for two projects approved previously; US$14.54 million was contracted for three projects; and US$11.28 million was disbursed to support 13 projects in implementation. A summary of annual financing activity for the past two years, as well as the overall status of the BEIF program at the end of 2017, is presented in Table 9.

TABLE 9:
BORDER ENVIRONMENT INFRASTRUCTURE FUND ANNUAL FINANCING ACTIVITY AND PROGRAM STATUS

(US$ Millions)

	2017	2016	Cumulative
EPA funding allocations:	**$ 8.96**	$ 9.56	$ 702.10
For projects	**7.82**	9.18	673.39
For program administration	**1.14**	0.38	28.71
Grants approved[1]	**6.24**	25.02	663.18
Grants contracted[1]	**14.54**	21.23	658.74
Grants disbursed	**11.28**	10.23	614.14
Contracted grants, not yet disbursed			$ 44.61
Approved grants, not yet contracted			4.44
Funding available for future projects[2]			10.21

[1] Annual and cumulative figures, less funds deobligated from completed or cancelled projects.
[2] EPA funding allocation for projects less grants approved.

For the years ended December 31, 2017 and 2016, NADB recognized US$799,248 and US$843,300, respectively, as reimbursement for administrative expenses incurred in running the program. Since program inception in 1997, NADB has been reimbursed US$23.06 million for administrative expenses, which represents 3.3% of the funds allocated by EPA to the program.

TECHNICAL ASSISTANCE

NADB Technical Assistance Program (TAP). With the approval of the Board of Directors, NADB may use a portion of its retained earnings to provide grants for technical assistance aimed at supporting border communities in the development of sustainable projects for certification and financing. Support may also be provided for sector studies to identify needs or generate knowledge about a new sector or technology, as well as for institutional capacity-building initiatives, such as the seminars offered through the Utility Management Institute (UMI). Since 2014, the TAP program has been jointly funded and administered with BECC.

During 2017, NADB approved US$831,500 in TAP grants to carry out 11 studies and other activities, including development of a state water plan for Chihuahua, emergency assistance to address transboundary sewer overflows in Naco, Sonora, and a preliminary engineering report and final design to repair a wastewater collector in Winterhaven, California. An additional US$335,000 from the annual UMI budget was committed to support the presentation of seven seminars in Mexico. Over the past five years, NADB has approved an average of US$983,894 annually in TAP grants and UMI funding to support technical assistance and capacity-building initiatives (Table 10).

As part of its funds management strategy for 2017, the Bank set a disbursement cap of US$1.50 million for this program. For the years ended December 31, 2017 and 2016, NADB disbursed US$781,502 and US$537,557, respectively, in grant funds for studies and training. Over the past five years, technical assistance disbursements have averaged US$789,417 annually (Table 10). These grants were funded with previously designated retained earnings, with the exception of UMI, which is budgeted on an annual basis.

For 2017 and 2016, no new funding was allocated to TAP from NADB's retained earnings; however, US$450,000 was budgeted in both years for UMI. As of December 31, 2017, NADB had a balance of US$3.18 million in retained earning designated to TAP, of which approximately US$1.03 million had been committed to specific studies. For 2018, the annual disbursement cap was set at US$1.55 million.

Many of NADB's technical assistance and training initiatives have been collaborative efforts jointly developed and funded with other public and private organizations. As part of its ongoing technical assistance strategy, NADB will continue to pursue partnerships with other entities aimed at creating synergies that support the development of environmentally sustainable and resilient border communities.

Administered Programs. In support of its environmental mandate, BECC administered two technical assistance programs funded with grants from EPA. Under the merger which went into effect on November 10, 2017, NADB signed novation agreements with EPA transferring administration of the programs and underlying grants to the Bank.

Project Development Assistance Program (PDAP). This program supports communities in the development of water and wastewater projects that have been prioritized to receive BEIF grants. EPA grant funds totaling US$3.41 million were transferred from BECC to the Bank. Under the terms of the grants, the Bank contracts consultants to perform studies and other project development activities and receives an allocation of the EPA grant funds for administrative expenses incurred. For the period November 10, 2017 through December 31, 2017, the Bank disbursed US$192,070 in technical assistance grants and recognized US$93,420 as reimbursement for administrative expenses incurred.

TABLE 10:
TECHNICAL ASSISTANCE ACTIVITIES 2013-2017

(US$ Thousands)

	2017	2016	2015	2014	2013
NADB PROGRAM					
Funding					
Approved	**$1,167**	$ 728	$1,070	$944	$1,018
Disbursed	**782**	538	1,179	759	690
Projects					
Activities approved[1]	**18**	22	28	11	14
Studies completed	**14**	4	1	2	3
Seminars held	**6**	15	9	7	10
PROGRAMS ADMINISTERED BY NADB					
Project Development Assistance Program [2]					
Funding approved	**$7**	$ -	$ -	$ -	$ -
Funding disbursed	**285**	-	-	-	-
Projects [3]					
Activities approved	**1**	-	-	-	-
Activities completed	**2**	-	-	-	-
U.S.-Mexico Border 2020 Program [2]					
Funding approved	**$300**	$ -	$ -	$ -	$ -
Funding disbursed	**75**	-	-	-	-
Projects [4]					
Activities approved	**4**	-	-	-	-
Activities completed	**1**	-	-	-	-

[1] Includes project development activities, training seminars and sector studies funded by NADB.

[2] Program funded with grants from the U.S. Enviornmental Protection Agency (EPA) and formerly administered by BECC. Figures reflect activity under NADB administration beginning as of November 10, 2017. Disbursements include technical assistance and administrative expenses.

[3] Includes project development studies and related activities, such as final design.

[5] Includes studies and workshops on topics related to clean air, safe drinking water, reduced risk of exposure to hazardous waste and emergency preparedness.

Border 2020: U.S.-Mexico Environmental Program. Through this program, EPA provides grants to support the joint efforts of the U.S. and Mexico governments to improve the environment and protect the health of residents within 100 kilometers of their shared border. EPA grant funds totaling US$2.19 million were transferred from BECC to the Bank. Under the terms of the grants, the Bank provides logistical and administrative services to facilitate meetings, as well as identifies, contracts and manages projects and workshops funded under the program. The Bank receives an allocation of the EPA grant funds for administrative expenses incurred. For the period November 10, 2017 through December 31, 2017, the Bank disbursed US$55,625 in technical assistance grants and recognized US$19,583 as reimbursement for administrative expenses incurred.

RESULTS OF OPERATIONS

The main source of revenue for NADB is derived from interest income on its loan portfolio and investment holdings. Expenses mainly consist of interest paid on borrowed funds and operating costs, which include provisions for loan losses. In 2017, the Bank had total revenue of US$68.62 million, while operating and interest expenses totaled US$40.09 million, providing net operating income of US$28.53 million. Table 11 provides a comparison of the main operating income and expenses for the years ended December 31, 2017 and 2016.

Net interest income. As indicated in the table below, net interest income decreased 5.3% in 2017 compared to the previous year, which is mainly attributable to a 25.8% increase in outstanding debt to comply with the liquidity policy and an 8.3% decrease in the loan portfolio. Nevertheless, interest income registered 10.2% growth over the previous year, as most of the US$117.49 million decline in the loan portfolio occurred during the last quarter of the year due to prepayments (US$113.22 million). In addition, investment holdings more than doubled from US$360.89 million to US$793.61 million during the year, mainly from the proceeds of debt issuances to cover liquidity requirements related to an upcoming bond payment and as a result of the loan prepayments. On the other hand, interest expense went up 58.6%, in part, because gross outstanding debt increased US$305.94 million to a total of US$1.49 billion and because of rising interest rates.

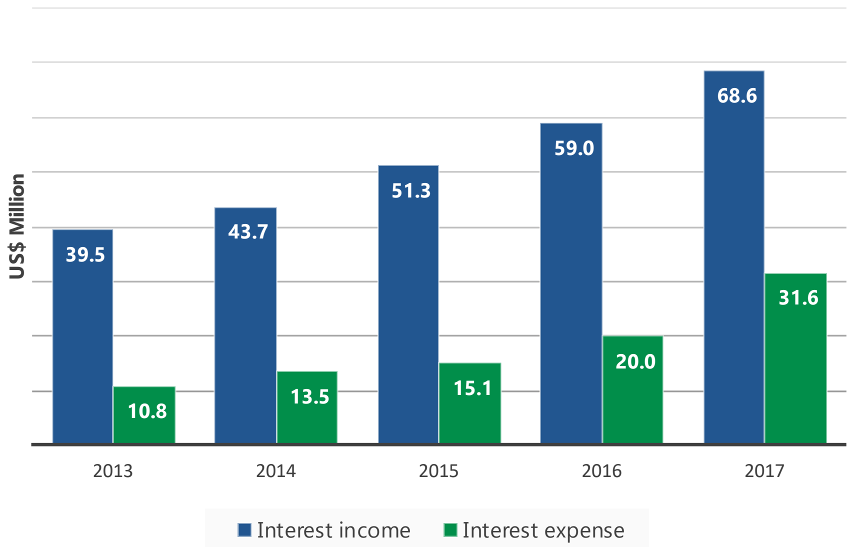
TABLE 11: OPERATING INCOME & EXPENSES

(US$ Millions)

	2017	2016	Difference
Loan interest income	**$ 57.76**	$ 52.43	$ 5.33
Investment interest income	**10.86**	6.58	4.28
	68.62	59.01	9.61
Interest expense	**31.64**	19.95	11.69
Net interest income	**36.98**	39.06	(2.08)
Operating expenses	**8.45**	17.93	(9.49)
Net operating income	**28.53**	21.13	7.41
Total non-interest income (and non-operating expenses)	**3.16**	(0.37)	3.53
Income before program activities	**$ 31.69**	$ 20.76	$ 10.93

Operating Expenses. Table 12 shows a comparison of the main operating expense categories for the years ended December 31, 2017 and 2016. Operating expenses in 2017 decreased by 52.9% compared to the previous year, mainly due to the US$3.94 million reduction in loan loss provision requirements in 2017 and a provision increase of US$5.13 million in 2016. The reduction in 2017 is derived from lower risks as more projects completed one year of operation, as well as from the smaller loan portfolio. The US$5.13 million increase in loan loss provisions in 2016 was partly due to the expansion of the general allowance policy to include public and public-private borrowers (US$1.89 million), as well as increased lending to private sector borrowers.

FIGURE 8:
INTEREST INCOME VS. INTEREST EXPENSE



Without the large differences in loan loss provisions, total operating expenses in 2017 reflect a 3.2% reduction compared to 2016. Expenses in the remaining categories remained relatively stable and were partially offset by US$1.25 million and US$420,467 in fees in 2017 and 2016, respectively. As a result of the merger, personnel and administrative expenses are expected to increase in 2018 with the addition of 40 employees and an office in Juarez, Chihuahua. These expenses will be mostly offset by budget contributions from the U.S. and Mexican governments, which formerly served as the main source of funding for BECC operations.

TABLE 12:
OPERATING EXPENSES

(US$ Millions)

Category	2017	2016	Difference
Personnel	**$ 8.38**	$ 8.28	$ 0.10
General & administrative	**1.63**	1.47	0.16
Consultants / contractors	**2.26**	2.72	(0.46)
Provision for loan losses	**(3.94)**	5.13	(9.08)
Depreciation	**0.17**	0.14	(0.18)
Other	**(0.04)**	0.19	(0.03)
Total	**$ 8.45**	$ 17.93	$ (9.49)

Non-interest income and non-operating expenses. This category mainly consists of non-cash transactions that are recorded on a mark-to-market basis, including net foreign exchange gains (losses) and net gains (losses) from swaps and other real estate owned, as well as net gains (losses) on sales of available-for-sale investment securities, loan fees and other miscellaneous income and expenses (Table 13). For the year ended December 31, 2017, the Bank recorded total non-interest income of US$3.16 million, mainly stemming from gains on sales and call of investment securities and increased fee income, compared to total non-operating expenses of US$368,984 the previous year.

TABLE 13:
NON-INTEREST INCOME AND NON-OPERATING EXPENSES

(US$ Millions)

Category	2017	2016
Gains on sales and call of investment securities	**$ 3.62**	$ 0.14
Net income (expense) from hedging activities	**(1.27)**	1.10
Net income (expense) from foreign exchange activities	**0.13**	(0.70)
Fees and other income	**0.68**	0.20
Loss on real estate owned	**-**	(1.11)
Total	**$ 3.16**	$ (0.37)

Program Expenses. These expenses consist of grant disbursements for studies, training and project implementation, which are funded with previously designated retained earnings, with the exception of UMI, which is budgeted on an annual basis. A breakdown of grant disbursements by program for the past two years is shown in Table 14. Over the past five years, grant disbursements have averaged US$2.27 million annually. More information about these programs, is provided under Grant Activity and Technical Assistance.

TABLE 14: PROGRAM EXPENSES

(US$ Millions)

Program	2017	2016
Community Assistance Program (CAP)	**$ 1.18**	$ 0.43
Water Conservation Investment Fund (WCIF) [1]	**0.20**	0.12
Technical Assistance Program (TAP) [2]	**0.55**	0.33
Utility Management Institute (UMI)	**0.23**	0.21
Total	**$ 2.16**	$ 1.09

1 This grant program was formally terminated in 2013. As of December 31, 2017, grant funds totaling US$95,594 were pending disbursement for the last WCIF project.
2 Excludes technical assistance funded by EPA or other sources.

FINANCIAL POSITION

EQUITY

As of December 31, 2017, total equity was US$634.31 million, an increase of 5.0% (US$30.28 million) compared to US$604.03 million at the close of 2016.

Capital. During 2017 there was no change in the capitalization of the Bank. In 2016, the Mexican and U.S. Governments each subscribed an additional 150,000 shares of capital stock of the Bank with a par value of US$10,000 per share, subject to the necessary legislation and availability of appropriations. The additional capital consists of 22,500 paid-in shares (US$225 million) and 127,500 callable shares (US$1.275 billion) from each country for a total of US$3.00 billion. Mexico made an initial contribution of US$10.00 million in paid-in capital in September 2016, along with the corresponding callable capital.

As of December 31, 2017 and 2016, NADB had US$415 million in paid-in capital, along with US$2,352 million in corresponding callable capital. A breakdown of the capital stock by source and type is provided in Table 15. Additional details about the capitalization of the Bank are provided in Note 7 of the consolidated financial statements.

TABLE 15: CAPITAL FUNDED*

(US$ Millions)

SOURCE	
Mexico	$ 1,416.67
United States	1,350.00
Total	$ 2,766.67
TYPE	
Paid-in	$ 415.00
Callable	2,351.67
Total	$ 2,766.67

* Excludes 10% of initial paid-in capital from each country (US$45 million total), along with the associated callable capital, which was allocated to domestic programs (see Note 8 of the consolidated financial statements).

Retained Earnings and Reserves. During 2017, retained earnings grew 19.9% to a total of US$207.54 million from US$173.06 million at the end of 2016 and are held in the General Reserve. This US$34.48 million increase includes US$4.96 million in BECC funds that were transferred to the Bank as a result of the merger and recorded as undesignated retained earnings.

In accordance with its retained earnings policy, NADB also maintains four specific reserves, which are described in Note 2 of the consolidated financial statements. Annual allocations from undesignated retained earnings to the reserve funds are made as necessary, and if available, to maintain the levels mandated under the policy. At the close of 2017 and 2016, all the reserves were fully funded.

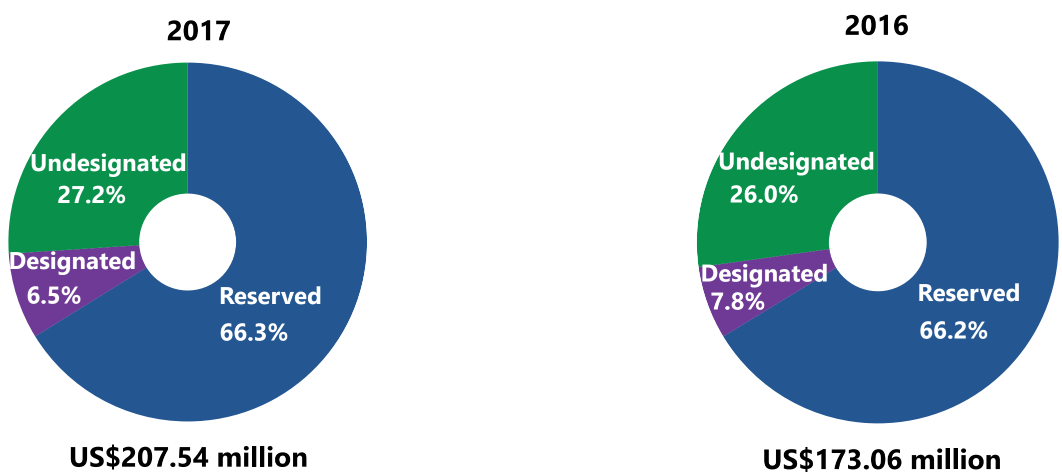
TABLE 16:
RESERVED AND DESIGNATED RETAINED EARNINGS
(US$ Millions)

	12/31/2017	12/31/2016
Reserved retained earnings		
Debt Service Reserve	**$ 42.00**	$ 30.80
Operating Expenses Reserve	**15.67**	13.37
Special Reserve*	**30.00**	30.00
Capital Preservation Reserve	**49.93**	40.37
Total reserved	**$ 137.60**	$ 114.54
Designated retained earnings		
Community Assistance Program (CAP)	**$ 10.25**	$ 8.81
Water Conservation Investment Fund (WCIF)	**0.09**	0.92
Technical Assistance Program (TAP)	**3.18**	3.73
Total designated	**$ 13.52**	$ 13.46

* This reserve may be used to offset losses on outstanding loans or to pay expenses relating to the enforcement of the Bank's rights under outstanding loan and guaranty agreements.

Table 16 provides a breakdown of the retained earnings allocated to reserves and programs at the end of 2017 and 2016. The amount allocated to reserves increased US$23.06 million (20.1%) in 2017, mainly because of debt service and capital preservation reserve requirements. During the same period, the amount designated to programs registered a net increase of US$65,814 (0.5%), deriving from the allocation of an additional US$2.00 million to the Community Assistance Program, which was offset by US$1.93 million in grant disbursements. With US$137.60 million in earnings allocated to reserves and US$13.52 million designated to fund programs, the Bank had US$56.42 million in undesignated retained earnings at the end of 2017, an increase of US$11.36 million (25.2%) over the balance at the end of 2016 (US$45.06 million).

FIGURE 9:
RETAINED EARNINGS DISTRIBUTION



DEBT

NADB leverages its funds by issuing debt in international capital markets or with other financial institutions for the purpose of financing its lending operations or refinancing existing borrowings. Its annual borrowing plan is reviewed and approved by the Board of Directors.

NADB borrowed US$311.20 million in 2017, compared to US$2.22 million in 2016. During 2017, the Bank issued a 10.5-year non-amortizing note in the Swiss capital market with a face value of CHF 125 million at a fixed coupon rate that generated proceeds of US$124.44 million, as well as a 15-year non-amortizing note in the Norwegian capital market with a face value of NOK 1,445 million at a fixed coupon rate that generated proceeds of US$173.45 million. Additionally, under a fixed-rate loan agreement for up to US$50 million contracted in November 2012 with the German development bank KfW, NADB drew down US$13.31 million to fund eligible wastewater projects in Mexico. The Bank did not issue any new debt in the capital markets during 2016; however, US$2.22 million was drawn down under the aforesaid loan agreement for Mexican wastewater projects.

Most of the debt was issued at fixed rates and in U.S. dollars, except for two fixed-rate issues in Swiss francs and one fixed-rate issue in Norwegian kroner. Most of the debt has been hedged through interest rate swaps, effectively changing it to floating rates. The three debt issues not denominated in U.S. dollars were hedged by cross-currency interest rate swaps, effectively changing them to floating rates in U.S. dollars. A breakdown of gross outstanding debt by type, currency and maturity is shown in Table 17.

In accordance with its debt limit policy, total debt outstanding may not exceed at any time the callable portion of the subscribed capital shares, plus the minimum liquidity level required under the liquidity policy. With US$2,352 million in subscribed callable capital and a minimum liquidity level of US$451.3 million, the maximum debt limit was US$2.803 billion, 9.5% higher than the maximum limit in 2016 (US$2.559 billion). At the close of 2017, total debt outstanding (US$1.493 billion) accounted for 53.3% of the debt limit.

TABLE 17:
GROSS DEBT
(US$ Millions)

	12/31/2017	12/31/2016
By Type		
Notes payable	**$ 1,456.60**	$ 1,158.71
Other borrowings	**36.84**	28.79
Total	**$ 1,493.44**	$ 1,187.50
By Currency		
U.S. dollars	**$ 1,066.84**	$ 1,058.79
Swiss francs	**253.15**	128.71
Norwegian kroner	**173.45**	-
Total	**$ 1,493.44**	$ 1,187.50
By Maturity		
Short term	**$ 305.26**	$ 5.26
Long term	**1,188.18**	1,182.24
Total	**$ 1,493.44**	$ 1,187.50

LIQUIDITY MANAGEMENT

NADB has established liquidity and investment policies to help ensure that it can meet its financial obligations at all times, even under conditions of constrained market access, as well as have sufficient cash flows to cover its operational needs in the normal course of business.

Under its liquidity policy, the Bank's minimum level of liquid holdings is equal to the highest consecutive 12 months of the following 18 months of expected debt service obligations, committed net loan disbursements and projected operating expenses for the relevant fiscal year. Minimum liquidity requirements are determined prior to the beginning of each fiscal year and may be revised during the year in the event of major changes in outlook. In accordance with this policy, the minimum liquidity balance for the 2017 fiscal year was set at US$151.3 million for the first four months of 2017 and in May was increased to US$451.3 million for the rest of the year to account for a US$300-million debt issue that matures in October 2018. To meet this liquidity requirement, NADB issued US$297.89 million in additional debt in March and April 2017. Liquidity remained above the required minimum level throughout the year.

For 2018, the minimum liquidity level will be US$553.5 million and, upon redemption of the aforesaid debt issuance in October 2018 and the funding of a US$250-million debt issuance that will mature in February 2020, the minimum liquidity level will decrease to US$503.5 million for the rest of the year.

The Bank's liquid asset holdings are in the form of cash, cash equivalents (mainly overnight repurchase agreements) and investments in longer term marketable securities (fixed-income securities). All investments held in the liquidity portfolio are designated as available-for-sale. As of December 31, 2017, 64.0% of the liquid asset portfolio was comprised of highly liquid assets (cash, cash equivalents and U.S. Treasuries). The remaining 36.0% was comprised of other types of liquid assets held by the Bank. A breakdown of the Bank's liquid assets at the close of 2017 and 2016 is provided in Table 18.

The portfolio of liquid assets more than doubled in 2017, increasing US$493.3 million over the prior-year balance. At the close of 2017, the Bank's liquid assets represented 44.3% of total assets (US$2,146 million) and 63.7% of total gross debt (US$1,493 million), as compared to 25.3% of total assets (US$1,813 million) and 38.6% of total gross debt (US$1,188 million) at the end of 2016.

TABLE 18:
LIQUID ASSETS
(US$ Millions)

Type of Security	12/31/2017	12/31/2016
Cash and cash equivalents	**$ 163.77**	$ 151.21
U.S. Treasury securities	**444.66**	117.33
U.S. agency securities	**123.59**	62.53
Mexican government securities (UMS)	**10.78**	11.54
Taxable municipal securities	**-**	0.25
Other permissible securities*	**208.25**	114.90
Total	**$ 951.05**	$ 457.77

* Other permissible securities include corporate debt securities, asset-backed securities, commercial paper and certificates of deposit.

The Bank manages its investment portfolio to ensure that its liquid assets are prudently invested to preserve capital and provide necessary liquidity, in compliance with the policies and guidelines approved by its Board. Under these policies, the Bank is restricted from investing more than 5% of its investment portfolio in the securities of any one issuer, excluding obligations of the U.S. Government, the Mexican Government and U.S. government agencies. The majority of the securities must be rated AA (or its equivalent) or higher by a recognized securities rating agency. There are only two exceptions: 1) Mexican government securities; and 2) corporate debt securities denominated in U.S. dollars and rated A (or its equivalent) or higher, which cannot exceed 25% of the total investment portfolio.

RISK MANAGEMENT

Given the nature of its business, NADB is subject to credit, market, liquidity and operational risks. The Bank has always operated within a conservative risk management framework in accordance with the provisions of the Charter and the policies approved by the Board of Directors. In 2014, the Bank established the Risk Management and Control Department to centralize the risk management function and continually assess and reinforce all aspects of its risk management strategies and tools.

CREDIT RISK

As a result of its core activity of providing environmental infrastructure loans, NADB is subject to potential losses arising from the failure of a borrower to pay principal and/or interest on a loan in accordance with the agreed-upon terms (loan portfolio credit risk), as well as from the possible default of an investment or swap counterparty (counterparty risk).

Loan Portfolio Credit Risk. To mitigate this risk, NADB has implemented several layers of protection. First, it has established prudent policies limiting its exposure per project and per obligor, as well as actively seeks to share the risk with other financial institutions. Secondly, the Bank follows a well-established loan review and structuring process based on a thorough analysis of the technical and financial characteristics of the project, as well as the managerial capacity and credit quality of the borrower. As part of this process all loan proposals must be reviewed and approved by the Funding Committee prior to submission to the Board. To support the Funding Committee's analysis, an expert advisor may be hired to provide an independent assessment of the potential risks associated with a given loan. Finally, the Bank continually monitors covenant compliance and the financial stability of each borrower throughout the term of the loan.

To further mitigate this credit default risk, all loans in the Bank's outstanding portfolio are secured by some form of credit support, such as project revenue, borrower cash flows, senior liens on project equity and assets, step-in rights or, in the case of loans to Mexican states and municipalities, federal tax revenue pledged to an irrevocable trust or pursuant to a mandate agreement. The Bank also maintains an allowance for loan losses, as well as a Special Reserve funded from its retained earnings, which are available to offset any losses on outstanding loans or pay expenses relating to the enforcement of the Bank's rights under outstanding loan agreements.

Counterparty Risk. The main sources of the Bank's counterparty risk are the financial instruments in which the Bank invests its liquidity and the swap transactions it enters into with a financial institution as the counterparty. The Bank maintains cash and cash equivalents, investments, and certain other financial instruments with various major financial institutions, performs periodic evaluations of their financial performance and relative credit standing, and limits the amount of credit exposure with any one institution. The criteria for selection of potential swap counterparties requires Board authorization, and NADB signs an International Swap and Derivatives Association (ISDA) agreement with appropriate collateral support provisions with the commercial banks with which it enters into swap transactions. As its hedging needs have evolved, the Bank has expanded its list of eligible counterparties with the dual purpose of allowing for price competition while simultaneously diversifying counterparty risk exposure. All swaps are currently with 10 counterparties, two of which are backed by the Government of Mexico. The other eight are commercial financial institutions with ratings ranging from AA to BBB from two internationally-recognized rating agencies, with some institutions having a split rating.

MARKET AND LIQUIDITY RISK

The Bank is exposed to market risks related to general market movements, mainly through fluctuations in interest and exchange rates affecting earnings on its loan and investment portfolios and the cost of its external borrowings. Liquidity risk arises from an inability to meet contractual obligations in a timely manner without adversely affecting the daily operations or the financial condition of the institution.

To mitigate market risks, NADB makes extensive use of financial derivatives, mainly interest-rate and cross-currency swaps, for the sole purpose of hedging its positions. Loans with repayment sources in Mexican pesos must be hedged to U.S. dollars (unless the source of funds is also in pesos), while fixed-rate loans and investments are mostly swapped to a variable rate.

To maintain adequate liquidity and protect the investment portfolio from significant losses caused by interest rate movements, the average duration of the portfolio may not exceed four years. Moreover, the Bank structures the portfolio so that its investment securities mature concurrent with anticipated cash flow requirements, with additional consideration for unanticipated cash demands. Additional information about the Bank's liquidity and investment policies is provided in the preceding section on Liquidity Management.

OPERATIONAL RISK

Operational risk is the potential loss arising from external events or from the inadequacy or failure of internal processes and systems or human error. It includes fraud and failures in the execution of legal, fiduciary and contractual responsibilities. These risks stem from the manner in which the Bank is operated, as opposed to the risk arising from its financial transactions. NADB manages its operational risk through a system of internal controls based on established policies and procedures for all significant areas of operation, including funds management, disbursements, procurement and financial reporting.

NADB is in the process of developing an Enterprise Resource Planning (ERP) system that will improve workflow and control mechanisms for administrative, financial and project processes under the merged institution. It consists of a suite of integrated applications that will collect, store, manage and interpret organizational data from all departments in order to provide a real-time integrated view of core business processes and the ability to report on the status of ongoing projects. The ERP system will boost operational efficiency, while also helping to mitigate risks related to human error. The first phase of the system will begin in early 2018.

In 2016, the Bank outsourced the internal audit function as a means of strengthening its operational framework with an emphasis on risk management. Garza/Gonzalez and Associates was selected through a competitive process to provide the internal audit services. During 2017, the firm audited five processes, including loan credit risk analysis, debt issuance and debt servicing. No significant findings were reported.

BASIS FOR REPORTING AND CRITICAL ACCOUNTING POLICIES

The consolidated financial statements of the Bank are prepared in accordance with generally accepted accounting principles (GAAP) in the United States and are consistent with that of an international organization. The notes to the financial statements contain a summary of NADB's significant accounting policies, including a discussion of recently issued rules and regulations. Certain of these policies are considered critical to the portrayal of the Bank's financial condition, because they require NADB management to make difficult, complex or subjective judgments, or relate to matters that are inherently uncertain. These policies include (i) the use of fair value accounting and (ii) the determination of the level of loss allowances in the loan portfolio.

Fair Value Accounting. The Bank uses fair value measurements to account for the value of its cross-currency interest rate swaps, interest rate swaps and available-for-sale debt securities. Where possible, fair value is determined by reference to quoted market prices. If quoted market prices are unavailable, then fair value is based on pricing and discounted cash flow models consistent with industry practices. The selection of data included in pricing and cash flow models involves a significant degree of judgment, and changes in the assumptions and measurements underlying this data could have a substantial impact on the amounts the Bank reports as assets and liabilities, as well as the related unrealized gains and losses reported on its income statement. The Bank believes that its estimates of fair value are reasonable in light of its established processes for obtaining data for use in its models; the periodic evaluation, review and validation of its models; and the consistent application of this approach from period to period. Additional information about this policy can be found in Notes 2 and 11 to the consolidated financial statements.

Loan Loss Allowances. The determination of the allowance for loan losses is based on management's current judgments about the credit quality of the loan portfolio, and the allowance is maintained at a level considered appropriate by management to provide for probable and estimable losses inherent in the loan portfolio. Determining the appropriate allowance for loan losses involves significant judgment about when a loss has been incurred and the amount of that loss. Actual losses may differ from expected losses due to unforeseen changes in a variety of factors that affect borrowers' creditworthiness and the accuracy of the Bank's allocated allowance. Additional information about this policy can be found in Notes 2 and 4 to the consolidated financial statements.

CONSOLIDATION

At the request of the U.S. Government, NADB holds and administers the funds of the U.S. Community Assistance and Investment Program (USCAIP or the U.S. Domestic Program) and, therefore, its accounts are consolidated with those of the Bank. However, the U.S. domestic program's operations and allocated capital are completely independent of those of the Bank, and any net income earned by the program and its profits, losses, expenses and disbursements do not affect the retained earnings or paid-in capital of the Bank. The supplementary information provided at the end of the consolidated financial statements includes combining statements that show the breakdown of NADB and USCAIP accounts. Additional information about the U.S. domestic program can be found in Note 8 to the consolidated financial statements.

EXTERNAL AUDITORS

The accounts of the Bank are audited annually by independent external auditors with established international experience chosen by the Board of Directors based on a proposal by Bank management. In accordance with the policies and principles established by the Board, the external auditors are selected through a competitive process, are appointed for terms of up to five years, and are engaged on an annual basis.

Ernst & Young LLP (E&Y) completed it second five-year term as the external auditor of the Bank in 2016. However, recognizing that the merger with BECC presented extraordinary circumstances that required an exception be made to the external auditor term limit in order to provide continuity in the audit process of the integrated institution and avoid substantially higher audit costs associated with a new firm familiarizing itself with both institutions individually and as a unified entity, the Board approved a two-year extension for E&Y that will end in 2018. The Bank renewed its contract with E&Y to carry out the annual audit of its accounts for fiscal year 2017.

CONSOLIDATED FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION

NORTH AMERICAN DEVELOPMENT BANK
YEARS ENDED DECEMBER 31, 2017 AND 2016
WITH REPORT OF INDEPENDENT AUDITORS

REPORT OF INDEPENDENT AUDITORS

Ernst & Young

The Board of Directors
North American Development Bank

We have audited the accompanying consolidated financial statements of North American Development Bank (the Bank), which comprise the consolidated balance sheets as of December 31, 2017 and 2016, and the related consolidated statements of income, comprehensive income, changes in equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in conformity with U.S. generally accepted accounting principles; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free of material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States. 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 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. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant 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 financial statements referred to above present fairly, in all material respects, the consolidated financial position of North American Development Bank at December 31, 2017 and 2016, and the consolidated results of its operations and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The Combining Balance Sheet by Program, Combining Statement of Income by Program, Combining Statement of Comprehensive Income by Program, Combining Statement of Cash Flows by Program, Statement of Income of NADB Office in Juarez, Chihuahua, and the Border Environment Infrastructure Fund are presented for purposes of additional analysis and are not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole.

Ernst & Young, LLP

San Antonio, Texas
March 29, 2018

CONSOLIDATED BALANCE SHEETS

	December 31	
	2017	**2016**
Assets		
Cash and cash equivalents:		
Held at other financial institutions in demand-deposit accounts	**$ 543,712**	$ 193,964
Held at other financial institutions in interest-bearing accounts	**26,742,869**	28,833,505
Repurchase agreements	**137,000,000**	122,700,000
	164,286,581	151,727,469
Held-to-maturity investment securities, at amortized cost	**3,904,396**	53,782,155
Available-for-sale investment securities, at fair value	**787,282,178**	306,562,226
Loans outstanding	**1,293,806,755**	1,411,625,673
Allowance for loan losses	**(21,107,945)**	(25,075,659)
Unamortized loan fees	**(11,711,140)**	(10,682,210)
Foreign currency exchange rate adjustment	**(45,997,351)**	(55,027,169)
Hedged items, at fair value	**(144,105,721)**	(151,854,451)
Net loans outstanding	**1,070,884,598**	1,168,986,184
Interest receivable	**28,781,647**	26,806,845
Grant and other receivable	**4,523,939**	7,320,234
Furniture, equipment and leasehold improvements, net	**354,961**	461,759
Other assets	**86,241,301**	98,029,324
Total assets	**$ 2,146,259,601**	$ 1,813,676,196
Liabilities and equity		
Liabilities:		
Accounts payable	**$ 6,749,106**	$ 7,456,087
Accrued liabilities	**1,385,789**	441,447
Accrued interest payable	**21,697,668**	16,593,968
Undisbursed grant funds	**1,002**	6,328
Short-term debt, net of discounts and unamortized debt issuance costs	**304,660,489**	5,262,000
Hedged items, at fair value	**(708,958)**	–
Net short-term debt	**303,951,531**	5,262,000
Long-term debt, net of discounts and unamortized debt issuance costs	**1,183,283,306**	1,176,158,912
Hedged items, at fair value	**(5,602,130)**	2,931,548
Net long-term debt	**1,177,681,176**	1,179,090,460
Total liabilities	**1,511,466,272**	1,208,850,290
Equity:		
Paid-in capital	**415,000,000**	415,000,000
General Reserve:		
Allocated paid-in capital	**2,338,897**	2,460,790
Retained earnings:		
Designated	**11,663,722**	11,780,134
Reserved	**137,602,160**	114,553,374
Undesignated	**56,416,631**	45,058,709
Accumulated other comprehensive income (loss)	**11,766,444**	15,967,278
Non-controlling interest	**5,475**	5,621
Total equity	**634,793,329**	604,825,906
Total liabilities and equity	**$ 2,146,259,601**	$ 1,813,676,196

The accompanying notes are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENTS OF INCOME

	Year Ended December 31	
	2017	**2016**
Interest income:		
Loans	**$ 57,770,501**	$ 52,430,015
Investments	**10,865,202**	6,586,686
Total interest income	**68,635,703**	59,016,701
Interest expense	**31,639,710**	19,950,461
Net interest income	**36,995,993**	39,066,240
Operating expenses:		
Personnel	**8,378,651**	8,282,656
General and administrative	**1,628,852**	1,467,292
Consultants and contractors	**2,260,139**	2,720,662
Provision for (recovery of) loan losses	**(3,967,714)**	5,133,737
Other	**(42,598)**	193,253
Depreciation	**167,382**	137,153
U.S. Domestic Program	**229,059**	268,461
Total operating expenses	**8,653,771**	18,203,214
Net operating income	**28,342,222**	20,863,026
Non-interest income and non-operating expenses:		
Gains on sales and call of securities	**3,616,047**	137,177
Income (expense) from hedging activities, net	**(1,266,924)**	1,101,921
Income (expense) from foreign exchange activities, net	**126,332**	(701,842)
Fees and other income	**680,696**	200,000
Loss on other real estate owned	**–**	(1,106,240)
Total non-interest income and non-operating expenses	**3,156,151**	(368,984)
Income before program activities	**31,498,373**	20,494,042
Program activities:		
Border Environment Infrastructure Fund (BEIF):		
U.S. Environmental Protection Agency (EPA) grant income	**799,248**	843,300
EPA grant administration expense	**(799,248)**	(843,300)
Community Assistance Program expense	**(1,178,056)**	(429,633)
Water Conservation Investment Fund expense	**(203,901)**	(120,808)
Technical Assistance Program:		
EPA grant income	**360,698**	–
EPA grant administration expense	**(113,003)**	–
Inter-American Development Bank (IDB) Multilateral Investment Fund (MIF) grant income	**16,808**	–
Technical assistance program expense	**(1,046,005)**	(537,557)
Net program expenses	**(2,163,459)**	(1,087,998)
Income before non-controlling interest	**29,334,914**	19,406,044
Net loss attributable to non-controlling interest	**(146)**	(142)
Net income attributable to NADB	**$ 29,335,060**	$ 19,406,186

The accompanying notes are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Year Ended December 31	
	2017	**2016**
Income before non-controlling interest	**$ 29,334,914**	$ 19,406,044
Net loss attributable to non-controlling interest	**(146)**	(142)
Net income attributable to NADB	**29,335,060**	19,406,186
Other comprehensive income (loss):		
Available-for-sale investment securities:		
Change in unrealized gains (losses) during the period, net	**(1,806,949)**	15,481
Reclassification adjustment for net gains (losses) included in net income	**(68,908)**	(137,177)
Total unrealized loss on available-for-sale investment securities	**(1,875,857)**	(121,696)
Foreign currency translation adjustment	**(39,664)**	158,889
Unrealized gains (losses) on hedging activities:		
Foreign currency translation adjustment, net	**9,029,818**	(11,580,208)
Fair value of cross-currency interest rate swaps, net	**(11,315,131)**	20,324,726
Total unrealized gain (loss) on hedging activities	**(2,285,313)**	8,744,518
Total other comprehensive income (loss)	**(4,200,834)**	8,781,711
Total comprehensive income	**$ 25,134,226**	$ 28,187,897

The accompanying notes are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Paid-in Capital	General Reserve: Allocated Paid-in Capital	General Reserve: Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Non-controlling Interest	Total Equity
Beginning balance, January 1, 2016	$ 405,000,000	$ 3,027,256	$ 151,986,031	$ 7,185,567	$ 5,763	$ 567,204,617
Capital contribution	10,000,000	–	–	–	–	10,000,000
Transfer to Targeted Grant Program of the U.S. Domestic Program	–	(566,466)	–	–	–	(566,466)
Net income	–	–	19,406,186	–	–	19,406,186
Other comprehensive income	–	–	–	8,781,711	–	8,781,711
Non-controlling interest	–	–	–	–	(142)	(142)
Ending balance, December 31, 2016	415,000,000	2,460,790	171,392,217	15,967,278	5,621	604,825,906
Capital contribution	**–**	**–**	**–**	**–**	**–**	**–**
Transfer to Targeted Grant Program of the U.S. Domestic Program	**–**	**(121,893)**	**–**	**–**	**–**	**(121,893)**
Transfer from the Border Environment Cooperation Commission (BECC)	**–**	**–**	**4,955,236**	**–**	**–**	**4,955,236**
Net income	**–**	**–**	**29,335,060**	**–**	**–**	**29,335,060**
Other comprehensive income	**–**	**–**	**–**	**(4,200,834)**	**–**	**(4,200,834)**
Non-controlling interest	**–**	**–**	**–**	**–**	**(146)**	**(146)**
Ending balance, December 31, 2017	**$ 415,000,000**	**$ 2,338,897**	**$ 205,682,513**	**$ 11,766,444**	**$ 5,475**	**$ 634,793,329**

The accompanying notes are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31	
	2017	**2016**
Operating activities		
Net income	**$ 29,335,060**	$ 19,406,186
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation	**167,382**	137,153
Amortization of net premium (discounts) on investments	**(363,450)**	907,746
Change in fair value of swaps, hedged items and other non-cash items	**(14,852,582)**	68,912,405
Non-controlling interest	**(146)**	(142)
Gains on sales of and call of securities, net	**(3,616,047)**	(137,177)
Provision for (recovery of) loan losses	**(3,967,714)**	5,133,737
Change in other assets and liabilities:		
Increase in interest receivable	**(1,974,802)**	(15,580,285)
(Increase) decrease in receivable and other assets	**2,669,963**	(4,813,027)
Increase (decrease) in accounts payable	**(706,981)**	5,643,003
Increase in accrued liabilities	**944,342**	91,427
Increase in accrued interest payable	**5,103,700**	7,514,503
Net cash provided by operating activities	**12,738,725**	87,215,529
Lending, investing, and development activities		
Capital expenditures	**(26,695)**	(342,452)
Loan principal repayments	**219,244,575**	49,762,528
Loan disbursements	**(101,425,657)**	(136,252,752)
Purchase of held-to-maturity investments	**(1,011,000)**	(2,261,000)
Purchase of available-for-sale investments	**(694,367,608)**	(240,224,271)
Proceeds from maturities and call of held-to-maturity investments	**54,457,031**	2,235,000
Proceeds from sales and maturities of available-for-sale investments	**212,183,024**	270,221,619
Net cash used in lending, investing, and development activities	**(310,946,330)**	(56,861,328)
Financing activities		
Capital contribution	**–**	10,000,000
Proceeds from other borrowings	**13,309,017**	2,216,528
Proceeds from note issuances	**297,891,683**	–
Principal repayment of other borrowings	**(5,262,000)**	(5,262,000)
Transfer of funds from Border Environment Cooperation Commission (BECC)	**4,955,236**	–
Grant funds from the Environmental Protection Agency (EPA)	**11,903,429**	10,650,006
Grant disbursements – EPA	**(11,908,755)**	(10,644,678)
Grant activity – U.S. Domestic Program	**(121,893)**	(566,466)
Net cash provided by financing activities	**310,766,717**	6,393,390
Net increase in cash and cash equivalents	**12,559,112**	36,747,591
Cash and cash equivalents at January 1, 2017 and 2016	**151,727,469**	114,979,878
Cash and cash equivalents at December 31, 2017 and 2016	**$ 164,286,581**	$ 151,727,469
Supplemental cash information		
Cash paid during the year for interest	**$ 30,977,485**	$ 30,730,491
Significant non-cash transactions		
Foreign currency translation adjustment	**$ 9,029,818**	$ (11,580,208)
Change in fair value of cross-currency interest rate swaps, net	**(11,315,131)**	20,324,726
Change in fair value of available-for-sales investments, net	**(1,875,857)**	(121,696)

The accompanying notes are an integral part of these consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2017

1. ORGANIZATION AND PURPOSE

The North American Development Bank (NADB or the Bank) and the Border Environment Cooperation Commission (BECC) were established on January 1, 1994 by an agreement between the Governments of the United States of America (the United States or U.S.) and the United Mexican States (Mexico) that was signed by their respective Presidents on November 16 and 18, 1993 (the Charter). The Bank was created to finance infrastructure projects in the U.S.-Mexico border region (the International Program) and community adjustment and investment projects throughout the U.S. and Mexico (the Domestic Programs). BECC was created to review the environmental aspects of projects seeking Bank financing under the International Program and recommend their certification to the Board of Directors. On March 16, 1994, the President of the United States issued an Executive Order designating the Bank as an international organization under the International Organization Immunities Act.

The Bank is governed by a Board of Directors appointed by the two countries. The operations of the Bank are subject to certain limitations outlined in the Charter. On November 10, 2017, the Second Protocol of Amendment to the Charter entered into force, merging BECC into the Bank. The merger preserved the mission, purposes and functions of both organizations under the International Program, including their environmental mandate and geographic jurisdiction, which is within 100 kilometers north of the U.S.-Mexico border and within 300 kilometers south of the border. The Bank is headquartered in San Antonio, Texas, and also has an office in Ciudad Juarez, Chihuahua (Juarez Office).

Under its International Program, the Bank provides loan and grant financing and technical assistance for infrastructure projects certified by the Board, as appropriate, and administers grant funding provided by other entities. Under the Domestic Programs, the Bank contributed funds from its equity to establish the domestic program of each country, and continues to administer the funds of the U.S. Domestic Program (see Note 8).

On June 2, 1998, the Board of Directors adopted a resolution authorizing the Bank to establish a limited-purpose financial institution (*sociedad financiera de objeto limitado*, SOFOL) for the purpose of facilitating Bank lending to the Mexican public sector. In January 1999, the *Corporación Financiera de América del Norte, S.A. de C.V. SOFOL* (COFIDAN) began operations in Mexico City and, in October 2006, COFIDAN was converted from a SOFOL to a non-regulated, multipurpose financial institution (SOFOM, E.N.R.), and its name was modified to *Corporación Financiera de América del Norte, S.A. de C.V. SOFOM E.N.R.* As of December 31, 2017, COFIDAN is 99.90% owned by the Bank and 0.10% owned by the Government of Mexico. The accounts of COFIDAN are consolidated with the Bank, and all material intercompany accounts and transactions are eliminated in the consolidation. The non-controlling interest reflected in the consolidated balance sheets and consolidated statements of income represents the ownership of the Government of Mexico through the Ministry of Finance and Public Credit (SHCP).

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation and Use of Estimates in Financial Statements

The financial statements have been prepared in conformity with U.S. generally accepted accounting principles (GAAP) and are presented in a manner consistent with that of an international organization. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. These estimates include the valuation of investments, allowance for loan losses, the fair value of derivative instruments and other real estate owned included in other assets, and the fair value of derivative instruments included in other liabilities and in long-term debt. Actual results could differ from those estimates.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Asset Acquisition – Border Environment Cooperation Commission (BECC) Integration

During 2017, the Bank adopted ASU 2017-01, which clarifies the definition of a business and provides a more robust framework to use in determining when a set of assets and activities constitutes a business. ASU 2017-01 is intended to provide guidance when evaluating whether transactions should be accounted for as an acquisition of assets or a business. The Bank determined that the transfer of assets from BECC on November 10, 2017 as described in Note 1 constituted an acquisition of assets under common control. As such, the assets of BECC were recorded at their carrying value and the operations of BECC were accounted for prospectively as of the merger date.

Principles of Consolidation

The consolidated financial statements include the accounts of the Bank and its subsidiary, COFIDAN. All significant intercompany accounts and transactions have been eliminated in consolidation.

Cash and Cash Equivalents

For purposes of the consolidated statements of cash flows, cash and cash equivalents include cash deposits with other financial institutions and overnight repurchase agreements.

Repurchase Agreements

The Bank has entered into agreements with two major financial institutions to purchase various U.S. government and federally sponsored agency securities under an agreement to resell. The purchase and resale of these securities occur daily, and the obligation to repurchase is backed by the assets of the related financial institutions. The underlying securities related to the repurchase transaction are held in the possession of the respective financial institutions.

Investment Securities

The Bank's investments are classified into the following categories:

> *Held-to-maturity* – This category is composed of those debt securities for which the Bank has the positive intent and ability to hold to maturity. These securities are carried at amortized cost.
>
> *Trading* – This category is composed of debt securities that are bought and held for resale in the near term. These securities are carried at fair value, and changes in market value are recognized in the consolidated statements of income.
>
> *Available-for-sale* – This category is composed of debt securities that are not classified as either trading or held-to-maturity securities. These securities are carried at fair value, with unrealized holding gains and losses excluded from earnings and reported as a net amount in a separate component of comprehensive income or loss until realized.

The accretion of discounts and the amortization of premiums are computed using the interest method. Realized gains and losses are determined using the specific identification method. Investments in a loss position are reviewed in order to determine whether the unrealized loss, which is considered an impairment, is temporary or other-than-temporary. In the event of other-than-temporary impairment, the cost basis of the investment would be written down to its fair value, and the credit component of the loss would be included in current earnings. The Bank had no securities classified as other-than-temporarily impaired as of December 31, 2017 and 2016.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Taxation

As an international organization, the Bank is exempt from all federal, state, and local taxation to the extent implemented by law under the U.S. International Organizations Immunities Act of 1945.

Furniture, Equipment, and Leasehold Improvements

Furniture and equipment are recorded at cost and depreciated over their estimated useful lives using the straight-line method. The estimated useful life is three years for computers and five years for furniture and other equipment. Leasehold improvements are recorded at cost and amortized over five years, or the life of the lease, whichever is less.

General Reserve

The Board of Directors defines the General Reserve as retained earnings plus allocated paid-in capital for the U.S. Domestic Program, as described in Note 8. Retained earnings are classified as either designated for a specific program, reserved, or undesignated. Undesignated retained earnings in excess of one percent (1.0%) of total assets of the International Program are used to fund four reserves in the following order of priority:

Debt Service Reserve – This reserve is maintained in an amount equal to 12 months of interest due on the Bank's outstanding debt at each fiscal year-end.

Operating Expenses Reserve – This reserve is maintained in an amount equal to 12 months of the operating budget expenses at each fiscal year-end.

Special Reserve – This reserve is maintained in an amount equal to the sum of: 1% of undisbursed loan commitments, 3% of the outstanding balance of disbursed loans and 3% of the outstanding balance of guaranties, less the general allowance for loan losses, with a targeted minimum of $30 million. Amounts in the Special Reserve are to be used to pay costs associated with the enforcement of the Bank's rights under its loan and guaranty agreements and to offset losses on any loan or guaranty.

Capital Preservation Reserve – This reserve is intended to maintain the value of the paid-in capital in real terms and is indexed to the U.S. annual inflation rate.

Loans and Allowance for Loan Losses

Loans are reported at the principal amount, net of allowance for loan losses, unamortized loan fees, foreign currency exchange rate adjustment and fair value of hedged items. Interest income on loans is recognized in the period earned. Net loan commitment and origination fees are deferred and amortized over the life of the loan as an adjustment to loan interest income.

Loans that are past due 90 days or more as to principal or interest, or where reasonable doubts exist as to timely collection, including loans that are individually identified as being impaired, are generally classified as nonperforming loans unless well secured and in the process of collection.

Loans are generally placed in nonaccrual status when principal or interest is delinquent for 180 days (unless adequately secured and in the process of collection) or circumstances indicate that the full collection of principal and interest is in doubt. When a loan is placed in nonaccrual status, accrued interest deemed uncollectible is either reversed (if current-year interest) or charged against current-year interest (if prior-year interest).

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Payments received on nonaccrual loans are generally applied to the recorded principal in the loan asset. If collection of the recorded principal in the loan is fully expected and the loan does not have a remaining unrecovered prior charge-off associated with it, payments are recognized as interest income. Nonaccrual loans may be returned to accrual status when contractual principal and interest are current, prior charge-offs have been recovered, the ability of the borrower to fulfill the contractual repayment terms is fully expected, and the loan is not classified as "doubtful" or "loss." If previously unrecognized interest income exists upon reinstatement of a nonaccrual loan to accrual status, interest income will only be recognized upon receipt of cash payments applied to the loan.

In cases where a borrower experiences financial difficulties and the Bank makes certain concessions to the borrower through modifications of the contractual terms of the loan, the loan is classified as a troubled debt restructuring. If the borrower's ability to meet the revised payment schedule is uncertain, the loan is classified as a nonaccrual loan.

The allowance for loan losses is a valuation account used to reasonably estimate loan losses incurred as of the financial statement date. Determining the appropriate allowance for loan losses involves significant judgment about when a loss has been incurred and the amount of that loss. A specific allowance is established for impaired loans when it is probable that the Bank may sustain some loss. Impairment of these loans is measured based on the present value of expected future cash flows, discounted at the loan's effective interest rate or the fair value of the collateral, if the loan is collateral-dependent. In 2013, under the International Program, a general allowance for loans to private-sector borrowers was established based on statistical cumulative default and recovery rates for project finance loans. In 2016, the general allowance methodology was expanded to include public and public-private borrowers.

The allowance for loan losses is maintained at a level considered appropriate by management to provide for probable and estimable losses inherent in the loan portfolio. The allowance is increased through provisions for loan losses and is decreased through recovery of loan losses and loan charge-offs. Upon final settlement of impaired loans, any remaining loss is charged off.

Credit Quality

The Bank monitors the credit quality of its loan portfolio on an ongoing basis by tracking certain credit quality indicators related to the borrower's: (i) payment history, (ii) strength of management, (iii) financial performance, (iv) appropriateness and effectiveness of project technology, and (v) loan covenant compliance, as well as (vi) general economic conditions in the borrower's geographic location, (vii) the legal and regulatory environment, and (viii) the effects, if any, of the current political environment. Based on this evaluation, each loan is assigned to one of the following risk categories:

Pass – The loan is not considered a greater than normal credit risk. The Bank believes the borrower has the ability to meet its obligations; therefore, the Bank anticipates insignificant uncollectible amounts.

Special Mention – The loan has exhibited potential weaknesses that deserve the Bank's close attention. If left uncorrected, these potential weaknesses may result in noticeable deterioration of the repayment prospects for the asset or of the borrower's credit position.

Substandard – The loan is inadequately protected by the current financial condition and paying capacity of the borrower or by any collateral pledged. The loan has a well-defined weakness or weaknesses that may jeopardize the collection of the debt pursuant to the contractual principal and interest terms. Such risk is characterized by the distinct possibility that the Bank may sustain some loss if the deficiencies are not corrected.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Doubtful – In addition to the risk characteristics described in the substandard category, the loan exhibits conditions and values that make collection or liquidation in full highly improbable. Loans in this risk category are closely managed to determine the highest recovery alternatives.

Program Activities

Grant income from the U.S. Environmental Protection Agency (EPA) associated with the Border Environment Infrastructure Fund (BEIF) represents reimbursed administrative expenses. Such amounts are earned and recognized as grant income in the accompanying consolidated statements of income as the associated expenses are incurred.

Grant income from EPA and other sources associated with technical assistance activities represent reimbursed administrative expenses and technical assistance grant disbursements funded by those entities. Such amounts are earned and recognized as grant income in the accompanying consolidated statements of income as the associated expenses are incurred.

Program expenses also represent grant disbursements funded with previously designated retained earnings of the Bank through its Community Assistance Program (CAP), Water Conservation Investment Fund (WCIF) and Technical Assistance Program. Grants are recognized at the date the Bank becomes obligated under the terms of the grant agreements, and associated costs are recognized as incurred.

EPA-funded BEIF grants and U.S. Domestic Program grant receipts and disbursements reflected in the consolidated statements of cash flows are not reflected in the accompanying consolidated statements of income, as these grants are approved and funded by the respective entities noted above. The Bank's role is to administer these funds

Foreign Currency

COFIDAN is located in Mexico and operates primarily using the local functional currency. Accordingly, all assets and liabilities of COFIDAN are translated using the exchange rate in effect at the end of the period, and revenue and costs are translated using average exchange rates for the period. The resulting cumulative translation adjustment is included in accumulated other comprehensive income.

The lending activities of the Bank include making loans that are denominated in Mexican pesos. For such loans, the Bank enters into cross-currency interest rate swaps that mitigate its exposure to fluctuations in foreign currency exchange rates and interest rates. As of December 31, 2017, the Bank had entered into swap counterparty agreements with *Fondo de Apoyo a Estados y Municipios* (FOAEM), a fund owned by the Government of Mexico and administered by the federally run development bank, *Banco Nacional de Obras y Servicios Publicos, S.N.C.* (Banobras); directly with Banobras outside the FOAEM arrangement; and with eight other financial institutions. The foreign currency translation adjustment on loans denominated in Mexican pesos as of December 31, 2017 and 2016 was $(45,997,351) and $(55,027,169), respectively. Changes in the foreign currency translation adjustment are reported through other comprehensive income.

All swaps relating to the lending activities of the Bank have been designated as cash flow or fair value hedges and are recognized in the accompanying consolidated balance sheets at their fair value. Changes in the fair value of the cash flow hedges are reported in other comprehensive income and are reclassified to earnings at the time of the hedged loan repayment. Changes in the fair value of the fair value hedges are reported as non-interest income or expense.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The Bank discontinues hedge accounting prospectively if it determines that the derivative is no longer highly effective in offsetting changes in the fair value or cash flows of the hedged item, or if it is no longer probable that the hedged loan repayment will occur. If hedge accounting is discontinued because the hedge ceases to be effective, the Bank will continue to record the swap at fair value with changes in value reflected in earnings for the period, and any fair value adjustments included in other comprehensive income will be recognized in the consolidated statements of income over the remaining life of the loan. If it is probable that the hedged loan repayments will not occur, gains and losses accumulated in other comprehensive income (loss) are recognized immediately in earnings.

Derivatives executed with all swap counterparties except for FOAEM are subject to a master netting arrangement. The net fair value of derivatives by counterparty is offset with the outstanding balance of the collateral received from or paid to the counterparty for financial reporting purposes. Additional information on the amounts subject to master netting arrangements and collateral is provided in Note 5.

Fair Value

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The Bank carries cross-currency interest rate swaps, interest rate swaps, hedged items, and available-for-sale debt securities at fair value. To determine the fair market value of its financial instruments, the Bank uses the fair value hierarchy, which is based on three levels of inputs as follows:

Level 1 – Quoted prices in active markets for identical assets or liabilities, which the reporting entity has the ability to access at the measurement date. This category generally includes U.S. government securities.

Level 2 – Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. This category generally includes U.S. agency securities, corporate debt securities, other fixed-income securities, United Mexican States (UMS) securities and mortgage-backed debt securities.

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant in determining the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation. This category includes cross-currency interest rate swaps, interest rate swaps, the fair value of hedged items and other real estate owned where independent pricing information is not available for a significant portion of the underlying assets. For these consolidated financial statements, the Bank also obtains dealer quotations for comparative purposes to assess the reasonableness of the pricing models.

Additional information on the fair value of the financial instruments of the Bank is provided in Note 11.

Accumulated Other Comprehensive Income

The components of other comprehensive income are reported in the accompanying consolidated statements of comprehensive income for all periods presented and in Note 7.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Reclassifications

Certain amounts in the prior year consolidated financial statements have been reclassified to conform to the current year consolidated financial statement presentation.

3. INVESTMENTS

All investments held by the Bank are classified as either held-to-maturity or available-for-sale securities. The following schedule summarizes investments as of December 31, 2017 and 2016.

		Gross Unrealized		
	Amortized Cost	Gains	Losses	Fair Value
December 31, 2017				
Held-to-maturity:				
U.S. agency securities	**$ 3,904,396**	**$ –**	**$ (31,912)**	**$ 3,872,484**
Mexican government securities (UMS)	**–**	**–**	**–**	**–**
Total held-to-maturity investment securities	**3,904,396**	**–**	**(31,912)**	**3,872,484**
Available-for-sale:				
U.S. government securities	**445,924,619**	**3,109**	**(1,270,425)**	**444,657,303**
U.S. agency securities	**124,224,160**	**56**	**(628,950)**	**123,595,266**
Corporate debt securities	**148,784,887**	**19,064**	**(462,854)**	**148,341,097**
Other fixed-income securities	**60,050,804**	**144**	**(143,036)**	**59,907,912**
Mexican government securities (UMS)	**10,721,127**	**74,734**	**(15,261)**	**10,780,600**
Total available-for-sale investment securities	**789,705,597**	**97,107**	**(2,520,526)**	**787,282,178**
Total investment securities	**$ 793,609,993**	**$ 97,107**	**$ (2,552,438)**	**$ 791,154,662**
December 31, 2016				
Held-to-maturity:				
U.S. agency securities	$ 3,868,082	$ 3,857	$ (23,507)	$ 3,848,432
Mexican government securities (UMS)	49,914,073	3,760,927	–	53,675,000
Total held-to-maturity investment securities	53,782,155	3,764,784	(23,507)	57,523,432
Available-for-sale:				
U.S. government securities	117,552,445	73,113	(299,703)	117,325,855
U.S. agency securities	62,587,782	176,961	(232,308)	62,532,435
Corporate debt securities	80,420,243	110,155	(240,116)	80,290,282
Other fixed-income securities	34,887,582	4,217	(34,100)	34,857,699
Mexican government securities (UMS)	11,661,736	4,957	(110,738)	11,555,955
Total available-for-sale investment securities	307,109,788	369,403	(916,965)	306,562,226
Total investment securities	$ 360,891,943	$ 4,134,187	$ (940,472)	$ 364,085,658

3. INVESTMENTS (CONTINUED)

The following schedule summarizes unrealized losses and the fair value of investments aggregated by category and the length of time individual securities have been in a continuous unrealized loss position as of December 31, 2017 and 2016.

	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2017						
Held-to-maturity:						
U.S. agency securities	**$ 3,872,484**	**$ 31,912**	**$ –**	**$ –**	**$ 3,872,484**	**$ 31,912**
Available-for-sale:						
U.S. government securities	**363,453,524**	**1,270,425**	**–**	**–**	**363,453,524**	**1,270,425**
U.S. agency securities	**122,603,016**	**628,950**	**–**	**–**	**122,603,016**	**628,950**
Corporate debt securities	**132,554,862**	**462,854**	**–**	**–**	**132,554,862**	**462,854**
Other fixed-income securities	**56,711,962**	**143,036**	**–**	**–**	**56,711,962**	**143,036**
Mexican government securities (UMS)	**3,527,600**	**15,261**	**–**	**–**	**3,527,600**	**15,261**
Total available-for-sale investment securities	**678,850,964**	**2,520,526**	**–**	**–**	**678,850,964**	**2,520,526**
Total temporarily impaired securities	**$ 682,723,448**	**$ 2,552,438**	**$ –**	**$ –**	**$ 682,723,448**	**$ 2,552,438**
December 31, 2016						
Held-to-maturity:						
U.S. agency securities	$ 2,767,178	$ 23,507	$ –	$ –	$ 2,767,178	$ 23,507
Available-for-sale:						
U.S. government securities	59,557,510	299,703	–	–	59,557,510	299,703
U.S. agency securities	19,363,071	232,308	–	–	19,363,071	232,308
Corporate debt securities	42,222,042	240,116	–	–	42,222,042	240,116
Other fixed-income securities	19,571,379	34,100	–	–	19,571,379	34,100
Mexican government securities (UMS)	7,817,425	110,738	–	–	7,817,425	110,738
Total available-for-sale investment securities	148,531,427	916,965	–	–	148,531,427	916,965
Total temporarily impaired securities	$ 151,298,605	$ 940,472	$ –	$ –	$ 151,298,605	$ 940,472

None of the unrealized losses identified in the preceding table are considered to be other-than-temporary since, as of December 31, 2017, the Bank did not have the intent to sell any of these securities and believed that it was more-likely-than-not that the Bank would not be required to sell any such securities before a recovery of cost.

3. INVESTMENTS (CONTINUED)

Contractual maturities of investments as of December 31, 2017 and 2016 are summarized in the following tables.

	Held-to-Maturity Securities		Available-for-Sale Securities	
	Fair Value	Amortized Cost	Fair Value	Amortized Cost
December 31, 2017				
Less than 1 year	**$ 1,171,872**	**$ 1,175,396**	**$ 651,270,945**	**$ 652,469,990**
1–5 years	**2,700,612**	**2,729,000**	**136,011,233**	**137,235,607**
5–10 years	**–**	**–**	**–**	**–**
More than 10 years	**–**	**–**	**–**	**–**
Mortgage-backed securities	**–**	**–**	**–**	**–**
	$ 3,872,484	**$ 3,904,396**	**$ 787,282,178**	**$ 789,705,597**
December 31, 2016				
Less than 1 year	$ 973,654	$ 974,685	$ 169,910,035	$ 169,947,758
1–5 years	56,549,778	52,807,470	136,652,191	137,162,030
5–10 years	–	–	–	–
More than 10 years	–	–	–	–
Mortgage-backed securities	–	–	–	–
	$ 57,523,432	$ 53,782,155	$ 306,562,226	$ 307,109,788

Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

The following table summarizes sale, call, and maturity activity of investment securities for the years ended December 31, 2017 and 2016.

	Year Ended December 31	
	2017	2016
Held-to-maturity investment securities:		
Proceeds from maturities and call	**$ 54,457,031**	$ 2,235,000
Gross realized gains from call	**3,547,139**	–
Available-for-sale investment securities:		
Proceeds from sales and maturities	**212,183,024**	270,221,619
Gross realized gains	**73,245**	137,290
Gross realized losses	**4,337**	113

3. INVESTMENTS (CONTINUED)

The following table sets forth the net unrealized gains (losses) on securities available-for-sale and the reclassification adjustments required for the years ended December 31, 2017 and 2016.

	2017	2016
Net unrealized losses on investment securities available-for-sale, beginning of year	**$ (547,562)**	$ (425,866)
Net unrealized gains (losses) on investment securities available-for-sale, arising during the year	**(1,806,949)**	15,481
Reclassification adjustments for net (gains) losses on investment securities available-for-sale included in net income	**(68,908)**	(137,177)
Net unrealized losses on investment securities available-for-sale, end of year	**$ (2,423,419)**	$ (547,562)

4. LOANS

The following schedule summarizes loans outstanding as of December 31, 2017 and 2016.

	International Program	U.S. Domestic Program	Total
December 31, 2017			
Loan balance	**$ 1,293,806,755**	**$ –**	**$ 1,293,806,755**
Allowance for loan losses:			
General	**(18,438,398)**	**–**	**(18,438,398)**
Specific	**(2,669,547)**	**–**	**(2,669,547)**
Unamortized loan fees	**(11,711,140)**	**–**	**(11,711,140)**
Foreign currency exchange rate adjustment	**(45,997,351)**	**–**	**(45,997,351)**
Fair value of hedged items	**(144,105,721)**	**–**	**(144,105,721)**
Net loans outstanding	**$ 1,070,884,598**	**$ –**	**$ 1,070,884,598**
December 31, 2016			
Loan balance	$ 1,411,295,846	$ 329,827	$ 1,411,625,673
Allowance for loan losses:			
General	(25,052,471)	(23,188)	(25,075,659)
Specific	–	–	–
Unamortized loan fees	(10,682,210)	–	(10,682,210)
Foreign currency exchange rate adjustment	(55,027,169)	–	(55,027,169)
Fair value of hedged items	(151,854,451)	–	(151,854,451)
Net loans outstanding	$ 1,168,679,545	$ 306,639	$ 1,168,986,184

4. LOANS (CONTINUED)

At December 31, 2017 and 2016, the International Program had outstanding unfunded loan commitments on signed loan agreements totaling $188,352,122 and $58,518,271, respectively. At those same dates, the U.S. Domestic Program did not have any outstanding loan commitments on signed loan agreements. The International Program also had loan agreements under development for an additional $136,140,220 as of December 31, 2017.

The Bank under certain circumstances offered below-market-rate loans. As of December 31, 2017 and 2016, the Bank had below-market-rate loans outstanding for the International Program of $35,847,009 and $39,675,001, respectively. At those same dates, the U.S. Domestic Program did not have any below-market-rate loans.

The following table presents the loan portfolio by sector as of December 31, 2017 and 2016.

	December 31	
	2017	**2016**
International Program:		
Air quality	**$ 95,634,593**	$ 103,691,911
Basic urban infrastructure	**37,093,463**	36,380,546
Clean energy:		
Solar	**291,197,939**	291,532,300
Wind	**620,669,578**	707,220,750
Other	**4,252,565**	4,823,929
Public transportation	**31,162,332**	31,865,601
Storm drainage	**52,715,102**	56,250,755
Water and wastewater	**161,081,183**	172,141,854
Water conservation	**–**	7,388,200
Total International Program	**1,293,806,755**	1,411,295,846
U.S. Domestic Program	**–**	329,827
	$ 1,293,806,755	$ 1,411,625,673

4. LOANS (CONTINUED)

The following table presents the loan portfolio by risk category as of December 31, 2017 and 2016. These risk categories are defined in Note 2, along with additional information on how the Bank evaluates credit quality.

	December 31	
	2017	**2016**
International Program		
Pass	**$ 1,279,427,547**	$ 1,394,063,313
Special Mention	**–**	–
Substandard	**14,379,208**	17,232,533
Doubtful	**–**	–
Total International Program	**1,293,806,755**	1,411,295,846
U.S. Domestic Program		
Pass	**–**	–
Special Mention	**–**	329,827
Substandard	**–**	–
Doubtful	**–**	–
Total U.S. Domestic Program	**–**	329,827
	$ 1,293,806,755	$ 1,411,625,673

There was one loan under the International Program on nonaccrual as of December 31, 2017 with an outstanding balance of $14,379,208 and no loans on nonaccrual as of December 31, 2016. As of December 31, 2017, this non-accrual loan had a specific allowance of $2,669,547. As of December 31, 2017 and 2016, the Bank had collateral valued at lower of cost or market from foreclosed loans reported as other assets of $3,104,639 and $2,978,307, respectively.

Under the U.S. Domestic Program, there were no loans outstanding as of December 31, 2017 and one loan was on non-accrual as of December 31, 2016 with an outstanding balance of $329,827.

The average impaired loan balance for the years December 31, 2017 and 2016 totals $9,155,761 and $343,043, respectively.

4. LOANS (CONTINUED)

An age analysis of past-due loans, including both accruing and non-accruing loans, as of December 31, 2017 and 2016, is shown in the following table.

	Loans 30–89 Days Past Due	Loans 90 or More Days Past Due	Total Past-due Loans
December 31, 2017			
International Program	**$ –**	**$ 14,379,208**	**$ 14,379,208**
U.S. Domestic Program	**–**	**–**	**–**
	$ –	**$ 14,379,208**	**$ 14,379,208**
December 31, 2016			
International Program	$ –	$ –	$ –
U.S. Domestic Program	–	329,827	329,827
	$ –	$ 329,827	$ 329,827

There were no loans past due 90 or more days accruing interest as of December 31, 2017 and 2016.

The following table summarizes the allowance for loan losses by classification as of December 31, 2017 and 2016.

	Allowance for Loan Losses			
	General Allowance	Specific Allowance	Total	Total Loans Outstanding
December 31, 2017				
International Program:				
Private:				
Construction	**$ 1,267,448**	**$ –**	**$ 1,267,448**	**$ 35,564,527**
Operation	**15,425,916**	**2,669,547**	**18,095,463**	**909,235,438**
Public	**1,262,795**	**–**	**1,262,795**	**252,558,904**
Public-private	**482,239**	**–**	**482,239**	**96,447,886**
Total International Program	**18,438,398**	**2,669,547**	**21,107,945**	**1,293,806,755**
U.S. Domestic Program	**–**	**–**	**–**	**–**
	$ 18,438,398	**$ 2,669,547**	**$ 21,107,945**	**$ 1,293,806,755**
December 31, 2016				
International Program:				
Private:				
Construction	$ 10,417,904	$ –	$ 10,417,904	$ 226,218,309
Operation	12,741,894	–	12,741,894	806,542,895
Public	1,441,539	–	1,441,539	288,307,752
Public-private	451,134	–	451,134	90,226,890
Total International Program	25,052,471	–	25,052,471	1,411,295,846
U.S. Domestic Program	23,188	–	23,188	329,827
	$ 25,075,659	$ –	$ 25,075,659	$ 1,411,625,673

Public-private refers to loans made to private-sector borrowers and backed by public-sector federal tax revenue.

4. LOANS (CONTINUED)

The following schedule summarizes the allowance for loan losses for the years ended December 31, 2017 and 2016.

	Allowance for Loan Losses				
		Loan Loss Provisions			
	Beginning Balance	Specific	General	Loan (Charge-offs) Recoveries	Ending Balance
December 31, 2017					
International Program:					
Private:					
Construction	**$ 10,417,904**	**$ –**	**$ (9,150,456)**	**$ –**	**$ 1,267,448**
Operation	**12,741,894**	**2,669,547**	**2,684,022**	**–**	**18,095,463**
Public	**1,441,539**	**–**	**(178,744)**	**–**	**1,262,795**
Public-private	**451,134**	**–**	**31,105**	**–**	**482,239**
Total International Program	**25,052,471**	**2,669,547**	**(6,614,073)**	**–**	**21,107,945**
U.S. Domestic Program	**23,188**	**–**	**(23,188)**	**–**	**–**
	$ 25,075,659	**$ 2,669,547**	**$ (6,637,261)**	**$ –**	**$ 21,107,945**
December 31, 2016					
International Program:					
Private:					
Construction	$ 10,300,322	$ –	$ 117,582	$ –	$ 10,417,904
Operation	9,618,412	–	3,123,482	–	12,741,894
Public	–	–	1,441,539	–	1,441,539
Public-private	–	–	451,134	–	451,134
Total International Program	19,918,734	–	5,133,737	–	25,052,471
U.S. Domestic Program	23,188	–	–	–	23,188
	$ 19,941,922	$ –	$ 5,133,737	$ –	$ 25,075,659

5. OTHER ASSETS

The following table presents the gross and net balances of other assets, including the result of master netting arrangements for derivatives with certain swap counterparties, at December 31, 2017 and 2016.

	Gross Amount	Master Netting Arrangements	Net Amount
December 31, 2017			
Cross-currency interest rate swaps	**$ 223,716,302**	**$ (22,102,844)**	**$ 201,613,458**
Interest rate swaps	**(4,690,552)**	**4,690,552**	**–**
Collateral from swap counterparties	**(117,380,000)**	**–**	**(117,380,000)**
Credit valuation adjustment for swaps	**(1,096,796)**	**–**	**(1,096,796)**
Other real estate owned	**3,104,639**	**–**	**3,104,639**
Total other assets	**$ 103,653,593**	**$ (17,412,292)**	**$ 86,241,301**
December 31, 2016			
Cross-currency interest rate swaps	$ 255,338,489	$ (27,619,486)	$ 227,719,003
Interest rate swaps	12,513,231	(8,447,465)	4,065,766
Collateral from swap counterparties	(135,490,000)	–	(135,490,000)
Credit valuation adjustment for swaps	(1,243,752)	–	(1,243,752)
Other real estate owned	2,978,307	–	2,978,307
Total other assets	$ 134,096,275	$ (36,066,951)	$ 98,029,324

6. DEBT

The following table summarizes the notes payable and other borrowings as of December 31, 2017 and 2016.

			December 31, 2017				
Issue Date	Maturity Date	Fixed Rate	Principal Amount	Unamortized Premium/ (Discount)	Unamortized Debt Issuance Costs	Fair Value of Hedged Items	Net Debt
Notes Payable							
USD Issuance							
02/11/10	02/11/20	4.375%	$ 250,000,000	$ (137,750)	$ (341,192)	$ 6,515,389	$ 256,036,447
10/26/12	10/26/22	2.400	250,000,000	(414,472)	(716,716)	(4,875,400)	243,993,412
12/17/12	10/26/22	2.400	180,000,000	(1,823,804)	(453,986)	(4,880,263)	172,841,947
12/17/12	12/17/30	3.300	50,000,000	–	(222,789)	(741,321)	49,035,890
10/10/13	10/10/18	2.300	300,000,000	(341,302)	(260,209)	(708,958)	298,689,531
CHF Issuance							
04/30/15	04/30/25	0.250	128,706,754	591,006	(609,166)	815,874	129,504,468
04/26/17	10/26/27	0.200	124,443,117	377,672	(609,049)	910,792	125,122,532
NOK Issuance							
03/10/17	03/10/32	2.470	173,448,566	28,666	(566,551)	(3,347,201)	169,563,480
Total notes payable			1,456,598,437	(1,719,984)	(3,779,658)	(6,311,088)	1,444,787,707
Other Borrowings							
08/15/13	06/30/18	1.900	2,631,000	–	–	–	2,631,000
08/15/13	12/30/18	1.900	600,467	–	–	–	600,467
04/11/14	12/30/18	1.900	2,030,533	–	–	–	2,030,533
04/11/14	06/30/19	1.900	2,631,000	–	–	–	2,631,000
04/11/14	12/30/19	1.900	2,632,000	–	–	–	2,632,000
04/11/14	06/30/20	1.900	526,785	–	–	–	526,785
08/14/14	06/30/20	1.900	2,105,215	–	–	–	2,105,215
08/14/14	12/30/20	1.900	2,632,000	–	–	–	2,632,000
08/14/14	06/30/21	1.900	1,008,985	–	–	–	1,008,985
02/13/15	06/30/21	1.900	1,623,015	–	–	–	1,623,015
02/13/15	12/30/21	1.900	1,470,635	–	–	–	1,470,635
07/29/15	12/30/21	1.900	1,161,365	–	–	–	1,161,365
07/29/15	06/30/22	1.900	266,455	–	–	–	266,455
09/16/16	06/30/22	1.900	2,216,528	–	–	–	2,216,528
03/17/17	06/30/22	1.900	149,017	–	–	–	149,017
03/17/17	12/30/22	1.900	2,632,000	–	–	–	2,632,000
03/17/17	06/30/23	1.900	2,632,000	–	–	–	2,632,000
03/17/17	12/30/23	1.900	2,632,000	–	–	–	2,632,000
03/17/17	06/30/24	1.900	2,632,000	–	–	–	2,632,000
03/17/17	12/30/24	1.900	2,170,720	–	–	–	2,170,720
11/13/17	12/30/24	1.900	461,280	–	–	–	461,280
Total other borrowings			36,845,000	–	–	–	36,845,000
			$1,493,443,437	$ (1,719,984)	$ (3,779,658)	$ (6,311,088)	$ 1,481,632,707

6. DEBT (CONTINUED)

			December 31, 2016				
Issue Date	Maturity Date	Fixed Rate	Principal Amount	Unamortized Premium/ (Discount)	Unamortized Debt Issuance Costs	Fair Value of Hedged Items	Net Debt
Notes Payable							
USD Issuance							
02/11/10	02/11/20	4.375%	$ 250,000,000	$ (203,000)	$ (502,811)	$ 11,844,826	$ 261,139,015
10/26/12	10/26/22	2.400	250,000,000	(500,472)	(865,430)	(3,429,048)	245,205,050
12/17/12	10/26/22	2.400	180,000,000	(2,202,230)	(548,185)	(4,130,413)	173,119,172
12/17/12	12/17/30	3.300	50,000,000	–	(239,978)	(888,004)	48,872,018
10/10/13	10/10/18	2.300	300,000,000	(400,402)	(595,962)	668,405	299,672,041
CHF Issuance							
04/30/15	04/30/25	0.250	128,706,754	666,880	(692,235)	(1,134,218)	127,547,181
Total notes payable			1,158,706,754	(2,639,224)	(3,444,601)	2,931,548	1,155,554,477
Other Borrowings							
08/15/13	06/30/17	1.900	2,631,000	–	–	–	2,631,000
08/15/13	12/30/17	1.900	2,631,000	–	–	–	2,631,000
08/15/13	06/30/18	1.900	2,631,000	–	–	–	2,631,000
08/15/13	12/30/18	1.900	600,467	–	–	–	600,467
04/11/14	12/30/18	1.900	2,030,533	–	–	–	2,030,533
04/11/14	06/30/19	1.900	2,631,000	–	–	–	2,631,000
04/11/14	12/30/19	1.900	2,632,000	–	–	–	2,632,000
04/11/14	06/30/20	1.900	526,785	–	–	–	526,785
08/14/14	06/30/20	1.900	2,105,215	–	–	–	2,105,215
08/14/14	12/30/20	1.900	2,632,000	–	–	–	2,632,000
08/14/14	06/30/21	1.900	1,008,985	–	–	–	1,008,985
02/13/15	06/30/21	1.900	1,623,015	–	–	–	1,623,015
02/13/15	12/30/21	1.900	1,470,635	–	–	–	1,470,635
07/29/15	12/30/21	1.900	1,161,365	–	–	–	1,161,365
07/29/15	06/30/22	1.900	266,455	–	–	–	266,455
09/16/16	06/30/22	1.900	2,216,528	–	–	–	2,216,528
Total other borrowings			28,797,983	–	–	–	28,797,983
			$ 1,187,504,737	$ (2,639,224)	$ (3,444,601)	$ 2,931,548	$ 1,184,352,460

Notes Payable

The notes payable are unsecured, rank equally with all other unsecured indebtedness, and cannot be redeemed prior to their maturity, at which time they will be redeemed at 100% of their principal amount. Interest payments are due semiannually or annually.

6. DEBT (CONTINUED)

The fair value of the hedges relating to interest rate swaps on a portion of the notes payable denominated in U.S. dollars was reported at December 31, 2017 as other assets of $(4,690,552) and other liabilities of $0 and at December 31, 2016 as other assets of $4,065,766 and other liabilities of $0. The fair value of the hedges relating to cross-currency interest rate swaps on notes payable not denominated in U.S. dollars was reported at December 31, 2017 as other assets of $301,562 and at December 31, 2016 as other assets of $(2,309,109). For additional information on the fair value of financial instruments and derivatives, see Notes 11 and 12.

Other Borrowings

On November 8, 2012, the Bank signed a loan commitment with another development bank to borrow up to $50 million to fund eligible projects in Mexico. This loan amortizes semiannually, with the first principal payment paid on December 30, 2015 and final principal payment due on December 30, 2024. As of December 31, 2017 and 2016, the outstanding balance was $36,845,000 and $28,797,983, respectively.

The following table summarizes the maturities of the notes payable and other borrowings as of December 31, 2017 and 2016.

	December 31	
	2017	**2016**
Less than 1 year	**$ 305,262,000**	$ 5,262,000
1–2 years	**5,263,000**	305,262,000
2–3 years	**255,264,000**	5,263,000
3–4 years	**5,264,000**	255,264,000
4–5 years	**435,264,000**	5,264,000
5–10 years	**263,677,871**	561,189,737
More than 10 years	**223,448,566**	50,000,000
Total	**$ 1,493,443,437**	$ 1,187,504,737

The following table summarizes short-term and long-term debt as of December 31, 2017 and 2016.

	December 31	
	2017	**2016**
Short-term debt:		
Notes payable	**$ 300,000,000**	$ –
Other borrowings	**5,262,000**	5,262,000
Total short-term debt	**305,262,000**	5,262,000
Long-term debt:		
Notes payable	**1,156,598,437**	1,158,706,754
Other borrowings	**31,583,000**	23,535,983
Total long-term debt	**1,188,181,437**	1,182,242,737
Total debt	**$ 1,493,443,437**	$ 1,187,504,737

7. EQUITY

Subscribed Capital

At December 31, 2017 and 2016, the Bank had subscribed 600,000 shares of capital stock, with a par value of $10,000 per share. As defined in the Charter, capital includes unqualified and qualified subscribed shares. Qualified subscribed shares are subject to the necessary legal requirements of each subscribing country. Unqualified subscribed shares have either been funded or authorized for purchase by the subscribing country. Capital is further classified as callable or paid-in capital at December 31, 2017 and 2016 as follows.

	Mexico		United States		Total	
	Shares	**Dollars**	**Shares**	**Dollars**	**Shares**	**Dollars**
Subscribed capital	300,000	$ 3,000,000,000	300,000	$ 3,000,000,000	600,000	$ 6,000,000,000
Less:						
Qualified callable capital	(121,833.3333)	(1,218,333,333)	(127,500)	(1,275,000,000)	(249,333.3333)	(2,493,333,333)
Unqualified callable capital	(133,166.6667)	(1,331,666,667)	(127,500)	(1,275,000,000)	(260,666.6667)	(2,606,666,667)
Qualified paid-in capital	(21,500)	(215,000,000)	(22,500)	(225,000,000)	(44,000)	(440,000,000)
Total funded paid-in capital	23,500	235,000,000	22,500	225,000,000	46,000	460,000,000
Less transfer to General Reserve for Domestic Programs	–	(22,500,000)	–	(22,500,000)	–	(45,000,000)
Total paid-in capital	23,500	$ 212,500,000	22,500	$ 202,500,000	46,000	$ 415,000,000

On May 6, 2016, Mexico submitted its letter of subscription to conditionally subscribe to 150,000 additional shares of capital stock with a par value of US$10,000 per share, subject to the necessary legal requirements and availability of appropriations. The capital stock is further classified as 22,500 qualified paid-in capital shares or US$225,000,000 and 127,500 qualified callable shares or US$1,275,000,000. On September 26, 2016, Mexico made its first contribution of the additional paid-in capital of $10,000,000 or 1,000 shares of paid-in capital and unqualified 5,666.6667 shares of callable capital.

On September 1, 2016, the United States submitted its letter of subscription to conditionally subscribe to 150,000 additional shares of capital stock with a par value of US$10,000 per share, subject to the necessary authorizing legislation and availability of appropriations. The capital stock is further classified as 22,500 qualified paid-in capital shares or US$225,000,000 and 127,500 qualified callable shares or US$1,275,000,000.

The subscriptions of members to paid-in capital and callable capital stock shall be in several installments, effective on or before December 31, 2016 through December 31, 2022, or such later dates as the Board of Directors shall determine. The callable portion of the subscription for capital shares of the Bank will be subject to call only when required to meet obligations, as outlined in Article II, Section 3(d), of Chapter II of the Charter.

7. EQUITY (CONTINUED)

Retained Earnings

Retained earnings are classified as designated, reserved, and undesignated by program, as follows:

	December 31	
	2017	**2016**
Designated retained earnings		
International Program:		
Water Conservation Investment Fund (WCIF)	**$ 95,594**	$ 918,920
Technical Assistance Program (TAP)	**3,175,828**	3,728,057
Community Assistance Program (CAP)	**10,252,839**	8,811,470
Total International Program	**13,524,261**	13,458,447
U.S. Domestic Program	**(1,860,539)**	(1,678,313)
Total designated retained earnings	**11,663,722**	11,780,134
Reserved retained earnings		
International Program:		
Debt Service Reserve	**42,000,000**	30,800,868
Operating Expenses Reserve	**15,669,072**	13,372,300
Special Reserve	**30,000,000**	30,000,000
Capital Preservation Reserve	**49,933,088**	40,370,311
Total International Program	**137,602,160**	114,543,479
U.S. Domestic Program:		
Special Reserve	**–**	9,895
Total reserved retained earnings	**137,602,160**	114,553,374
Undesignated retained earnings		
International Program:		
Operations	**53,548,372**	40,472,593
Mark-to-market hedge valuations	**2,868,259**	4,586,116
Total undesignated retained earnings	**56,416,631**	45,058,709
Total retained earnings	**$ 205,682,513**	$ 171,392,217
Retained earnings by program		
International Program	**$ 207,543,052**	$ 173,060,635
U.S. Domestic Program	**(1,860,539)**	(1,668,418)
Total retained earnings	**$ 205,682,513**	$ 171,392,217

Additional information regarding the reserved funds and each program listed above is provided in Notes 2 and 9, respectively.

With the integration on November 10, 2017, BECC transferred to the Bank total assets of $5,202,963, consisting of $4,620,931 in cash and cash equivalents, $33,889 in furniture and equipment, net of accumulated depreciation, and $548,143 in grant and other receivables. Along with the transferred assets, BECC also transferred accrued liabilities of $247,727 and undesignated retained earnings of $4,955,236. These funds have been recorded on the consolidated balance sheet as of December 31, 2017.

7. EQUITY (CONTINUED)

Accumulated Other Comprehensive Income

The following table presents the changes in accumulated other comprehensive income (loss) for the years ended December 31, 2017 and 2016.

	Beginning Balance	Period Activity	Ending Balance
December 31, 2017			
Unrealized loss on available-for-sale investment securities	**$ (547,562)**	**$ (1,875,857)**	**$ (2,423,419)**
Foreign currency translation adjustment	**373,108**	**(39,664)**	**333,444**
Unrealized gain (loss) on hedging activities:			
Foreign currency translation adjustment	**(55,027,169)**	**9,029,818**	**(45,997,351)**
Fair value of cross-currency interest rate swaps	**71,168,901**	**(11,315,131)**	**59,853,770**
Net unrealized gain (loss) on hedging activities	**16,141,732**	**(2,285,313)**	**13,856,419**
Total accumulated other comprehensive income (loss)	**$ 15,967,278**	**$ (4,200,834)**	**$ 11,766,444**
December 31, 2016			
Unrealized loss on available-for-sale investment securities	$ (425,865)	$ (121,696)	$ (547,561)
Foreign currency translation adjustment	214,219	158,889	373,108
Unrealized gain (loss) on hedging activities:			
Foreign currency translation adjustment	(43,446,961)	(11,580,208)	(55,027,169)
Fair value of cross-currency interest rate swaps	50,844,174	20,324,726	71,168,900
Net unrealized gain on hedging activities	7,397,213	8,744,518	16,141,731
Total accumulated other comprehensive income (loss)	$ 7,185,567	$ 8,781,711	$ 15,967,278

8. DOMESTIC PROGRAMS

As specified in the Charter, 10% of each country's initial subscription of capital stock was set aside to finance community adjustment and investment programs. In accordance with the Charter, the Board of Directors approved transfers in prior years of $45,000,000, equal to 10% of the initial paid-in capital of $450,000,000 from the initial subscription, to the General Reserve to support these programs. To further clarify operations related to these programs, the Bank entered into a Memorandum of Understanding (MOU) with each country. In accordance with the MOUs, the U.S. and Mexican programs are administered independently.

Mexico

The MOU with Mexico specified that 10% of the initial paid-in capital from its initial capital subscription and the related earnings be set aside for the community adjustment and investment program endorsed by Mexico. The Government of Mexico instituted its domestic program, entitled *Programa Complementario de Apoyo a Comunidades y Empresas* (Mexican Domestic Program), through the offices of SHCP. In June 1996, SHCP entered into a mandate agreement with Banobras to receive and administer the funds allocated for this program. The Mexican Domestic Program funds were fully transferred to Mexico as of June 1999. Accordingly, the activities of the Mexican Domestic Program are not reflected as operations of the Bank.

United States

The MOU with the U.S. Government specified that 10% of the initial paid-in capital from its initial capital subscription and the related earnings be set aside for the U.S. Community Adjustment and Investment Program (U.S. Domestic Program). The Bank provides financing endorsed by the Finance Committee appointed by the U.S. Government for that purpose.

8. DOMESTIC PROGRAMS (CONTINUED)

In accordance with the Charter and MOU with the United States, net assets of the Bank in the amounts of $478,358 and $792,372 were designated for the U.S. Domestic Program at December 31, 2017 and 2016, respectively. The revenue related to these amounts for the years ended December 31, 2017 and 2016 was $13,750 and $5,161, respectively. Additionally, expenses directly related to the operation of the U.S. Domestic Program of $229,059 and $268,461, are included in the operations of the Bank for the years ended December 31, 2017 and 2016, respectively. All expenses and disbursements are paid out of the U.S. Domestic Program funds. Deficit retained earnings on the U.S. Domestic Program capital funds as of December 31, 2017 and 2016, were $1,860,539 and $1,668,418, respectively. Under the U.S. Domestic Program, $511,160 in cash and cash equivalents was available for disbursement as of December 31, 2017.

In January 2009, the Finance Committee approved a Targeted Grant Program (TGP) to be funded with the remaining balance of the U.S. Domestic Program's allocated paid-in capital. As of December 31, 2017 and 2016, the U.S. Domestic Program's allocated paid-in capital totaled $2,338,897 and $2,460,790, respectively. For the years ended December 31, 2017 and 2016, $121,893 and $566,466, respectively, were disbursed through the TGP. These disbursements were reported as a deduction from allocated paid-in capital.

9. PROGRAM ACTIVITIES

Program activities are comprised of the following:

	Year Ended December 31	
	2017	**2016**
Program income:		
Border Environment Infrastructure Fund (BEIF)		
EPA grant income	**$ 799,248**	$ 843,300
Technical Assistance Program:		
EPA grant income		
Project Development Assistance Program (PDAP)	**285,490**	–
U.S.-Mexico Border 2020 Program (Border 2020)	**75,208**	–
IDB Multilateral Investment Fund (MIF) grant income	**16,808**	–
Total program income	**1,176,754**	843,300
Program expenses:		
BEIF		
EPA grant administration	**799,248**	843,300
Community Assistance Program	**1,178,056**	429,633
Water Conservation Investment Fund	**203,901**	120,808
Technical Assistance Program:		
NADB technical assistance and training expense	**781,502**	537,557
EPA grant administration	**113,003**	–
EPA grant expense – PDAP	**192,070**	–
EPA grant expense – Border 2020	**55,625**	–
IDB-MIF grant expense	**16,808**	–
Total program expenses	**3,340,213**	1,931,298
Net program expenses	**$ 2,163,459**	$ 1,087,998

9. PROGRAM ACTIVITIES (CONTINUED)

Border Environment Infrastructure Fund (BEIF)

The Bank administers grant funds from EPA through the BEIF. EPA grant awards since the initial grant made in April 1997 to December 31, 2017, total $701,772,141. Under the terms of the grants, the Bank reviews and submits prospective projects to EPA, which approves the projects. EPA then disburses funds to the Bank, which directs the grant monies to the specified project. The Bank also oversees progress and compliance requirements for EPA and receives an allocation of the EPA grant funds for administrative expenses incurred.

As of December 31, 2017, EPA has approved project funding proposed by the Bank totaling $663,176,432, of which $614,135,401 has been disbursed through the Bank. The Bank recognized $799,248 and $843,300 as reimbursement of expenses incurred for the years ended December 31, 2017 and 2016, respectively. These funds have been recorded as program revenue and expenses in the consolidated statements of income.

Water Conservation Investment Fund (WCIF)

In August 2002, the Board of Directors established the WCIF to finance water conservation projects in the U.S.-Mexico border region and designated $80,000,000 of the Bank's undesignated retained earnings to the program. Of that amount, $40,000,000 was reserved exclusively for water conservation projects in each country. For the years ended December 31, 2017 and 2016, $203,901 and $120,808, respectively, were disbursed under this fund. As of December 31, 2017, cumulative disbursements total $38,239,378 for the United States and $39,990,407 for Mexico. These disbursements were funded with previously designated retained earnings and have been reported as a program expense.

In May 2013, the Board agreed to close out the WCIF and transfer any uncommitted funds to the CAP program. As of December 31, 2017, a cumulative total of $1,674,621 in uncommitted WCIF funds was transferred to the CAP program.

Community Assistance Program (CAP)

In February 2011, the Board of Directors approved a grant program to support public projects in all sectors eligible for Bank financing. The CAP program is funded from the Bank's undesignated retained earnings as authorized by the Board. As of December 31, 2017, a cumulative total of $14,092,840 has been allocated to the CAP. For the years ended December 31, 2017 and 2016, $1,178,056 and $429,633, respectively, were disbursed under this program. These disbursements were funded with previously designated retained earnings and have been reported as a program expense.

Technical Assistance Program

The Bank uses a portion of its retained earnings as authorized by the Board of Directors to offer technical assistance and training to project sponsors for the purpose of strengthening their financial performance and ensuring the long-term sustainability of their infrastructure. Through the TAP, assistance is provided in three categories: project development, institutional capacity-building measures, and sector studies to identify needs and generate knowledge about a new sector or technology. For the years ended December 31, 2017 and 2016, $552,229 and $327,082, respectively, was disbursed under this program. These disbursements were funded with previously designated retained earnings and have been reported as a program expense.

As part of its technical assistance program, the Utility Management Institute (UMI) provides water utility managers and their staff with an opportunity for ongoing professional development aimed at enhancing their managerial and financial skills. For the years ended December 31, 2017 and 2016, $229,273 and $210,475, respectively, was expended under this program.

9. PROGRAM ACTIVITIES (CONTINUED)

Additionally, the Bank administers grant funds for technical assistance provided by other entities as follows:

Project Development Assistance Program (PDAP) – The PDAP program was administered previously by BECC. Since November 10, 2017, the date of integration, the Bank administers grants from EPA, on a reimbursement basis, to assist communities in the development of water and wastewater projects that have been prioritized by EPA to receive BEIF grants. The Bank recognized $192,070 in technical assistance expense and $93,420 in grant administrative expense for the period from November 10, 2017 to December 31, 2017. These funds have been recorded as program revenue and expenses in the consolidated statement of income.

U.S.-Mexico Border 2020 Program – The Border 2020 program was administered previously by BECC. Since November 10, 2017, the date of integration, the Bank administers grant funds from EPA, on a reimbursement basis, to support joint efforts of the two governments to improve the environment and protect the health of residents within 100 kilometers of the U.S.-Mexico border. The Bank provides logistical and administrative services to facilitate meetings, as well as identify, contract and manage projects and workshops funded under the program. The Bank recognized $55,625 in technical assistance expense and $19,583 in grant administrative expense for the period from November 10, 2017 to December 31, 2017. These funds have been recorded as program revenue and expenses in the consolidated statement of income.

Multilateral Investment Fund (MIF) Grant – The MIF grant was administered previously by BECC. Since November 10, 2017, the date of integration, the Bank administers grant funds provided by MIF, on a reimbursement basis, to support the development and implementation of a sustainable e-waste management and recycling system in Mexicali, Baja California. The Bank recognized $16,808 in technical assistance expense for the period from November 10, 2017 to December 31, 2017. These funds have been recorded as program revenue and expenses in the consolidated statement of income.

10. EMPLOYEE BENEFITS

401(a) Retirement Plan

The Bank has a 401(a) Retirement Plan for its employees. This plan provides for employee and nondiscretionary employer contributions. For the years ended December 31, 2017 and 2016, the Bank expended $814,344 and $751,187, respectively, relating to the plan.

Retiree Health Insurance Plan

The Bank has a retiree health insurance plan for qualifying employees based on number of years of service and age. Qualified retirees may purchase group health insurance coverage at the current employee rate subject to plan limits.

11. FAIR VALUE OF FINANCIAL INSTRUMENTS

Information on how the Bank measures fair value and classifies the levels of the fair value inputs is provided in Note 2.

Cash and Cash Equivalents

The carrying amounts for cash and cash equivalents approximate their fair value.

Securities Held-to-Maturity

Securities classified as held-to-maturity are reported at amortized costs. The fair value of these securities is estimated using Level 2 observable inputs. For these securities, the Bank obtains fair value measurements from an independent pricing service, which are based on prices quoted for a similar instrument.

Securities Available-for-Sale

Securities classified as available-for-sale are reported at fair value using Level 1 and Level 2 observable inputs. For these securities, the Bank obtains fair value measurements from an independent pricing service, which are based on prices quoted for the exact or like-kind instrument.

Loans Receivable and Interest Receivable

The fair value of loans is estimated based on Level 2 observable inputs using discounted cash flow analyses and interest rates currently being offered for loans made by the Bank with similar terms to borrowers of similar credit quality, net of allowance for loan loss. The fair value of nonaccrual loans is estimated to equal the aggregate net realizable value of the underlying collateral and guaranties. The carrying amount of accrued interest approximates its fair value. This valuation does not consider liquidity discounts currently being used by certain market participants, since measuring their impact would not be cost-beneficial for the Bank, given the nature of its loan portfolio.

Hedged Items for Loans

Hedged items for loans are reported at fair value using Level 3 unobservable inputs. The fair value of these hedged items is estimated by discounting each cash flow stream using the benchmark swap curve of the contractual currency and converting the resulting net present value at the spot exchange rate, as well as using external pricing models and counterparty pricing. Cash flows in Mexican pesos are discounted using the Mexico Benchmark Interbank Deposit Rate (TIIE) 28-day swap curve. Cash flows in U.S. dollars are discounted using the USD Overnight Index Swap (OIS) curve.

Cross-currency Interest Rate Swaps

Cross-currency interest rate swaps are reported at fair value using Level 3 unobservable inputs. The fair value of these swaps is estimated based on discounting procedures, whereby each cash flow stream is discounted using the benchmark swap curve of the respective currency and converting the resulting net present value at the spot exchange rate, as well as external pricing models and counterparty pricing. The Bank's cross-currency interest rate swaps are all Mexican-peso for U.S.-dollar operations except for three (3) debt issuances in foreign currencies for U.S.-dollar operations. Cash flows in Mexican pesos are discounted using the TIIE 28-day swap curve. Cash flows in Swiss francs (CHF) are discounted using the CHF swap curve. Cash flows in Norwegian krone (NOK) are discounted using the NOK swap curve. Cash flows in U.S. dollars are discounted using the USD OIS curve.

11. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

Interest Rate Swaps

Interest rate swaps are reported at fair value using Level 3 unobservable inputs. The fair value of these swaps is estimated based on discounting procedures, whereby each cash flow stream is discounted using the USD OIS curve, as well as external pricing models and counterparty pricing.

Other Real Estate Owned

Other real estate owned is reported at fair value using Level 3 unobservable inputs based on customized discounting criteria.

Debt and Accrued Interest Payable

Notes payable and other borrowings are carried at amortized cost. The fair value of the debt is estimated based on Level 2 observable inputs by discounting the cash flow stream using the USD OIS curve. The carrying amount of accrued interest payable approximates its fair value.

Hedged Items for Notes Payable

Hedged items for notes payable are reported at fair value using Level 3 unobservable inputs. The fair value of the hedged items is estimated based on discounting procedures, whereby each cash flow stream is discounted using the USD OIS curve for USD issuances, the CHF swap curve for the Swiss franc issuance and the NOK swap curve for the Norwegian krone issuance, as well as on external pricing models and counterparty pricing.

The following table summarizes the carrying amounts and fair value of the Bank's financial instruments.

	December 31, 2017		December 31, 2016	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Assets				
Cash and cash equivalents	**$ 164,286,581**	**$ 164,286,581**	$ 151,727,469	$ 151,727,469
Held-to-maturity securities	**3,904,396**	**3,872,484**	53,782,155	57,523,432
Available-for-sale securities	**787,282,178**	**787,282,178**	306,562,226	306,562,226
Loans, net	**1,070,884,598**	**1,110,949,537**	1,168,986,184	1,200,398,847
Interest receivable	**28,781,647**	**28,781,647**	26,806,845	26,806,845
Cross-currency interest rate swaps	**206,304,010**	**206,304,010**	227,719,003	227,719,003
Interest rate swaps	**(4,690,552)**	**(4,690,552)**	4,065,766	4,065,766
Other real estate owned	**3,104,639**	**3,104,639**	2,978,307	2,978,307
Liabilities				
Accrued interest payable	**21,697,668**	**21,697,668**	16,593,968	16,593,968
Short-term debt, net	**304,660,489**	**304,660,489**	5,262,000	5,262,000
Long-term debt, net	**1,183,283,306**	**1,183,863,120**	1,176,158,912	1,178,937,246

11. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

The Bank's financial assets and liabilities measured at fair value on a recurring basis as of December 31, 2017 and 2016 are summarized in the following table by the valuation level of the inputs used to measure fair value. Additional information on how the Bank measures and classifies the levels of fair-value inputs is provided in Note 2.

	Fair Value Measurements Using			
	Level 1	**Level 2**	**Level 3**	**Total Fair Value**
December 31, 2017				
Assets				
Available-for-sale (AFS) securities:				
U.S. government securities	**$ 444,657,303**	**$ –**	**$ –**	**$ 444,657,303**
U.S. agency securities	**–**	**123,595,266**	**–**	**123,595,266**
Corporate debt securities	**–**	**148,341,097**	**–**	**148,341,097**
Other fixed-income securities	**–**	**59,907,912**	**–**	**59,907,912**
Mexican government securities (UMS)	**–**	**10,780,600**	**–**	**10,780,600**
Total AFS securities	**444,657,303**	**342,624,875**	**–**	**787,282,178**
Cross-currency interest rate swaps	**–**	**–**	**206,304,010**	**206,304,010**
Interest rate swaps	**–**	**–**	**(4,690,552)**	**(4,690,552)**
Hedged items for loans	**–**	**–**	**(144,105,721)**	**(144,105,721)**
Total assets at fair value	**$ 444,657,303**	**$ 342,624,875**	**$ 57,507,737**	**$ 844,789,915**
Liabilities				
Cross-currency interest rate swaps	**$ –**	**$ –**	**$ –**	**$ –**
Interest rate swaps	**–**	**–**	**–**	**–**
Hedged items for notes payable	**–**	**–**	**(6,311,088)**	**(6,311,088)**
Total liabilities at fair value	**$ –**	**$ –**	**$ (6,311,088)**	**$ (6,311,088)**
December 31, 2016				
Assets				
Available-for-sale (AFS) securities:				
U.S. government securities	$ 117,325,855	$ –	$ –	$ 117,325,855
U.S. agency securities	–	62,532,435	–	62,532,435
Corporate debt securities	–	80,290,282	–	80,290,282
Other fixed-income securities	–	34,857,699	–	34,857,699
Mexican government securities (UMS)	–	11,555,955	–	11,555,955
Total AFS securities	117,325,855	189,236,371	–	306,562,226
Cross-currency interest rate swaps	–	–	227,719,003	227,719,003
Interest rate swaps	–	–	4,065,766	4,065,766
Hedged items for loans	–	–	(151,854,451)	(151,854,451)
Total assets at fair value	$ 117,325,855	$ 189,236,371	$ 79,930,318	$ 386,492,544
Liabilities				
Cross-currency interest rate swaps	$ –	$ –	$ –	$ –
Interest rate swaps	–	–	–	–
Hedged items for notes payable	–	–	2,931,548	2,931,548
Total liabilities at fair value	$ –	$ –	$ 2,931,548	$ 2,931,548

11. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

The following table summarizes the changes to the financial assets and liabilities measured at fair value on a recurring basis using unobservable inputs (Level 3) during the years ended December 31, 2017 and 2016. Additional information on how the Bank measures fair value is provided in Note 2.

	Fair Value of Level 3 Instruments		
	Cross-currency Interest Rate Swaps	Interest Rate Swaps	Hedged Items
Assets			
Beginning balance, January 1, 2017	**$ 227,719,003**	**$ 4,065,766**	**$ (151,854,451)**
Total realized and unrealized gains (losses):			
Included in earnings (expenses)	**(12,635,914)**	**(4,065,766)**	**7,748,730**
Included in other comprehensive income (loss)	**(11,315,131)**	**–**	**–**
Purchases	**–**	**–**	**–**
Settlements	**(2,154,500)**	**–**	**–**
Transfers in/out of Level 3	**–**	**–**	**–**
Ending balance, December 31, 2017	**$ 201,613,458**	**$ –**	**$ (144,105,721)**
Beginning balance, January 1, 2016	$ 106,695,082	$ 15,727,245	$ (51,606,468)
Total realized and unrealized gains (losses):			
Included in earnings (expenses)	100,699,195	(11,661,479)	(100,247,983)
Included in other comprehensive income	20,324,726	–	–
Purchases	–	–	–
Settlements	–	–	–
Transfers in/out of Level 3	–	–	–
Ending balance, December 31, 2016	$ 227,719,003	$ 4,065,766	$ (151,854,451)
Liabilities			
Beginning balance, January 1, 2017	**$ –**	**$ –**	**$ 2,931,548**
Total realized and unrealized (gains) losses:			
Included in (earnings) expenses	**–**	**–**	**(9,242,636)**
Included in other comprehensive income	**–**	**–**	**–**
Purchases	**–**	**–**	**–**
Settlements	**–**	**–**	**–**
Transfers in/out of Level 3	**–**	**–**	**–**
Ending balance, December 31, 2017	**$ –**	**$ –**	**$ (6,311,088)**
Beginning balance, January 1, 2016	$ 2,395,365	$ 3,815,603	$ 10,180,086
Total realized and unrealized (gains) losses:			
Included in (earnings) expenses	(2,395,365)	(3,815,603)	(7,248,538)
Included in other comprehensive income	–	–	–
Purchases	–	–	–
Settlements	–	–	–
Transfers in/out of Level 3	–	–	–
Ending balance, December 31, 2016	$ –	$ –	$ 2,931,548

11. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

The Bank entered into seven (7) cross-currency interest rate swaps and three (3) interest rate swaps during the year ended December 31, 2017. Upon issuance, the fair value of the swaps is $0 and, therefore, is not portrayed in the purchases line item in the preceding table. The change in fair value of these instruments is included within the total gains (losses) line item.

The Bank has no nonfinancial assets or liabilities measured at fair value on a recurring basis. Certain nonfinancial assets and liabilities measured at fair value on a nonrecurring basis include foreclosed assets (upon initial recognition or subsequent impairment) and other nonfinancial long-lived assets measured at fair value for impairment assessment. The fair value of the collateral from foreclosed loans is measured using Level 3 unobservable inputs and is reported in other assets as other real estate owned of $3,104,639 and $2,978,307 at December 31, 2017 and 2016, respectively. For the years ended December 31, 2017 and 2016, the Bank did not remeasure any existing real estate owned and did not record any impairment of long-lived assets.

12. DERIVATIVE FINANCIAL INSTRUMENTS

The Bank utilizes cross-currency interest rate swaps to mitigate exposure to fluctuations in foreign currency exchange rates and interest rate swaps to mitigate exposure to fluctuations in interest rates. The fair value of the swaps outstanding as of each reporting period end is included in other assets or other liabilities, depending on whether the Bank is in a favorable or unfavorable position as of the reporting period date.

The Bank enters into cross-currency interest rate swaps that are matched to specific fixed, variable, or adjustable rate loans denominated in Mexican pesos that the Bank has entered into directly with the borrower or with COFIDAN. In the latter case, COFIDAN then enters into loans denominated in Mexican pesos under the exact same terms with its borrowers. The Bank has also entered into cross-currency interest rate swaps for its long-term notes payable issued in Swiss francs and Norwegian krones. These swaps have been designated as hedging instruments because they hedge the risk of fluctuations in cash flows due to changes in foreign currency exchange rates. The swaps are structured so that the notional amounts mature to match the expected maturity of the loans and the notes payable.

The Bank enters into interest rate swaps that are matched to the terms of loans and to a portion of its long-term notes payable. The swaps have been designated as hedging instruments, because they hedge the risk of changes in the fair value of fixed-rate loans and notes payable due to changes in the designated benchmark interest rate. The Bank designated the LIBOR swap rate as the benchmark interest rate. The swaps are structured so that the notional amounts mature to match the expected maturity of the loans and the notes payable.

Under its arrangement with FOAEM, neither the Bank nor the counterparty is required to post collateral to support the outstanding fair value of the swaps. Beginning in July 2009, under counterparty relationships with other financial institutions, collateral may be required to be posted by either the Bank or the counterparty. Cash collateral of $117,380,000 and $135,490,000 was posted from counterparties to the Bank as of December 31, 2017 and 2016, respectively. No collateral was posted by the Bank as of December 31, 2017 and 2016.

12. DERIVATIVE FINANCIAL INSTRUMENTS (CONTINUED)

The notional amounts and estimated fair values of the swaps outstanding at December 31, 2017 and 2016 are presented in the following table. The fair value of these swaps is estimated using internal valuation models with observable market data inputs.

	December 31, 2017		December 31, 2016	
	Notional Amount	Estimated Fair Value, Net	Notional Amount	Estimated Fair Value, Net
Cross-currency interest rate swaps	**$ 934,856,215**	**$ 206,304,010**	$ 655,539,583	$ 227,719,003
Interest rate swaps	**1,318,431,886**	**(4,690,552)**	1,326,246,801	4,065,766

The referenced exchange rate received for the cross-currency interest rate swaps outstanding at December 31, 2017 and 2016 was 5.09% and 4.82%, respectively.

Swaps that are no longer deemed effective because of borrower default on the hedged loans are not included in the preceding table. There were no swaps that were considered ineffective due to borrower default as of December 31, 2017 and 2016.

Gains and Losses on Derivative Cash Flows

Cross-currency Interest Rate Swaps – The effective portion of the gain or loss due to changes in the fair value of cross-currency interest rate swaps designated as cash flow hedges is included in the accompanying consolidated statements of comprehensive income, while the ineffective portion is included in income (expense) from net hedging activities. The accumulated gain (loss) is reclassified into earnings as the hedged cash flows are received to offset the foreign currency gains (losses) that would have been recognized in earnings if the Bank had not been a party to the swaps. The accumulated net gain (loss) related to the swaps included in accumulated other comprehensive income totaled $13,856,419 and $16,141,732 at December 31, 2017 and 2016, respectively.

Gains or losses due to changes in the fair value of cross-currency interest rate swaps designated as fair value hedges and ineffective swaps are reported in income (expense) from net hedging activities. For the years ended December 31, 2017 and 2016, changes in the aforementioned swaps included in the accompanying consolidated statements of income were $(1,393,658) and $1,447,745, respectively.

Interest Rate Swaps – With regard to the interest rate swaps on outstanding loans and a portion of the long-term notes payable, the changes in the fair value of the swaps offset the changes in the fair value of the loans and debt due to changes in the USD OIS curve, while the ineffective portion is included in income (expense) from net hedging activities. For the years ended December 31, 2017 and 2016, changes in the aforementioned swaps included in the accompanying consolidated statements of income were $0 and $394,267, respectively.

13. CREDIT RISK ASSOCIATED WITH FINANCIAL INSTRUMENTS

The Bank is subject to certain credit risk. Financial instruments that potentially subject the Bank to significant concentrations of credit risk consist principally of cash and cash equivalents, investments, loans receivable and swaps. The Bank maintains cash and cash equivalents, investments and certain other financial instruments with various major financial institutions. The Bank performs periodic evaluations of the relative credit standing of these financial institutions and limits the amount of credit exposure with any one institution. The Bank evaluates the creditworthiness of each customer on a case-by-case basis and continually monitors the financial stability of each borrower.

14. COMMITMENTS

In the normal course of business, the Bank has various outstanding commitments, in addition to the loans receivable disclosed in Note 4 and the long-term borrowings disclosed in Note 6. Under agreements with consultants and contractors in effect at December 31, 2017, the Bank has obligations to make payments contingent upon the future performance of the consultants and contractors under the terms of their respective contracts and, therefore, they are not recorded in the financial statements.

Lease Commitments

The Bank rents office space under an operating lease that expires on February 28, 2026. Rent expense totaled $211,364 and $102,563 for the years ended December 31, 2017 and 2016, respectively. The following schedule summarizes the minimum future expenses for the forgoing lease.

Year Ended		
December 31, 2018	$	211,792
December 31, 2019		214,231
December 31, 2020		221,831
December 31, 2021		223,064
December 31, 2022		241,712
Thereafter		752,782
	$	1,865,412

15. ACCOUNTING STANDARDS UPDATES

Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers (Topic 606)*. ASU 2014-09 implements a common revenue standard that clarifies the principles for recognizing revenue. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that core principle, an entity should apply the following steps: (i) identify the contract(s) with a customer, (ii) identify the performance obligations in the contract, (iii) determine the transaction price, (iv) allocate the transaction price to the performance obligations in the contract and (v) recognize revenue when (or as) the entity satisfies a performance obligation. ASU 2014-09 is effective for the Bank on January 1, 2019. The Bank does not anticipate a significant impact to its consolidated financial statements since the primary source of revenue is interest income from loans and investments, which does not fall within the scope of this ASU.

ASU 2016-01, *Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. ASU 2016-1, among other things, (i) requires equity investments, with certain exceptions, to be measured at fair value with changes in fair value recognized in net income, (ii) simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment, (iii) eliminates the requirement for public business entities to disclose the methods and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet, (iv) requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes, (v) requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when

15. ACCOUNTING STANDARDS UPDATES (CONTINUED)

the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments, (vi) requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset on the balance sheet or the accompanying notes to the financial statements and (vii) clarifies that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities. ASU 2016-1 will be effective for the Bank on January 1, 2019 and is not expected to have a significant impact on the Bank's consolidated financial statements.

ASU 2016-02, *Leases (Topic 842)*. ASU 2016-02, among other things, require lessees to recognize a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis and a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. ASU 2016-02 does not significantly change lease accounting requirements applicable to lessors; however, certain changes were made to align, where necessary, lessor accounting with the lessee accounting model and ASC Topic 606: Revenue from Contracts with Customers. ASU 2016-02 will be effective for the Bank on January 1, 2020 and will require transition using a modified retrospective approach for leases existing at or entered into after, the beginning of the earliest comparative period presented in the financial statements. Notwithstanding the foregoing, in January 2018, the Financial Accounting Standards Board issued a proposal to provide an additional transition method that would allow entities to not apply the guidance in ASU 2016-02 in the comparative periods presented in the financial statements and instead recognize a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. The Bank is evaluating the potential impact of ASU 2016-02 to its consolidated financial statements and disclosures.

ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments.* ASU 2016-13 requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts and requires enhanced disclosures related to the significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an organization's portfolio. In addition, ASU 2016-13 amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. ASU 2016-13 will be effective for the Bank on January 1, 2021. The Bank is evaluating the potential impact of ASU 2016-13 to its consolidated financial statements.

ASU 2017-12, *Derivatives and Hedging (Topic 815) – Targeted Improvements to Accounting for Hedging Activities.* ASU 2017-12 amends the hedge accounting recognition and presentation requirements in ASC 815 to improve the transparency and understandability of information conveyed to financial statement users about an entity's risk management activities to better align the entity's financial reporting for hedging relationships with those risk management activities and to reduce the complexity of and simplify the application of hedge accounting. ASU 2017-12 will be effective for the Bank on January 1, 2020 and is not expected to have a significant impact on its financial statements

16. SUBSEQUENT EVENTS

The Bank has evaluated subsequent events for potential recognition and/or disclosure through March 29, 2018, the date these consolidated financial statements were issued.

SUPPLEMENTARY INFORMATION

COMBINING BALANCE SHEET BY PROGRAM

DECEMBER 31, 2017

	International Program	U.S. Domestic Program (A)	Eliminations	Total
Assets				
Cash and cash equivalents:				
Held at other financial institutions in demand deposit accounts	$ 543,712	$ –	$ –	$ 543,712
Held at other financial institutions in interest-bearing accounts	26,531,709	211,160	–	26,742,869
Repurchase agreements	136,700,000	300,000	–	137,000,000
	163,775,421	511,160	–	164,286,581
Held-to-maturity investment securities, at amortized cost	3,904,396	–	–	3,904,396
Available-for-sale investment securities, at fair value	787,282,178	–	–	787,282,178
Loans outstanding	1,293,806,755	–	–	1,293,806,755
Allowance for loan losses	(21,107,945)	–	–	(21,107,945)
Unamortized loan fees	(11,711,140)	–	–	(11,711,140)
Foreign currency exchange rate adjustment	(45,997,351)	–	–	(45,997,351)
Hedged items, at fair value	(144,105,721)	–	–	(144,105,721)
Net loans outstanding	1,070,884,598	–	–	1,070,884,598
Interest receivable	28,781,598	49	–	28,781,647
Grant and other receivable	4,523,939	–	–	4,523,939
Due from U.S. Domestic Program	4,688	–	(4,688)	–
Furniture, equipment and leasehold improvements, net	354,961	–	–	354,961
Other assets	86,241,301	–	–	86,241,301
Total assets	$ 2,145,753,080	$ 511,209	$ (4,688)	$ 2,146,259,601
Liabilities and equity				
Liabilities:				
Accounts payable	$ 6,749,106	$ –	$ –	$ 6,749,106
Accrued liabilities	1,357,626	28,163	–	1,385,789
Due to International Program	–	4,688	(4,688)	–
Accrued interest payable	21,697,668	–	–	21,697,668
Undisbursed grant funds	1,002	–	–	1,002
Short-term debt, net of discounts and unamortized debt issuance costs	304,660,489	–	–	304,660,489
Hedged items, at fair value	(708,958)	–	–	(708,958)
Net short-term debt	303,951,531	–	–	303,951,531
Long-term debt, net of discounts and unamortized debt issuance costs	1,183,283,306	–	–	1,183,283,306
Hedged items, at fair value	(5,602,130)	–	–	(5,602,130)
Net long-term debt	1,177,681,176	–	–	1,177,681,176
Total liabilities	1,511,438,109	32,851	(4,688)	1,511,466,272
Equity:				
Paid-in capital	415,000,000	–	–	415,000,000
General Reserve:				
Allocated paid-in capital	–	2,338,897	–	2,338,897
Retained earnings:				
Designated	13,524,261	(1,860,539)	–	11,663,722
Reserved	137,602,160	–	–	137,602,160
Undesignated	56,416,631	–	–	56,416,631
Accumulated other comprehensive income	11,766,444	–	–	11,766,444
Non-controlling interest	5,475	–	–	5,475
Total equity	634,314,971	478,358	–	634,793,329
Total liabilities and equity	$ 2,145,753,080	$ 511,209	$ (4,688)	$ 2,146,259,601

Note A – The Mexican Domestic Program funds were fully transferred to Mexico as of June 1999.

COMBINING STATEMENT OF INCOME BY PROGRAM

YEAR ENDED DECEMBER 31, 2017

	International Program	U.S. Domestic Program (A)	Total
Interest income:			
Loans	$ 57,761,188	$ 9,313	$ 57,770,501
Investments	10,860,765	4,437	10,865,202
Total interest income	68,621,953	13,750	68,635,703
Interest expense	31,639,710	–	31,639,710
Net interest income	36,982,243	13,750	36,995,993
Operating expenses:			
Personnel	8,378,651	–	8,378,651
General and administrative	1,628,852	–	1,628,852
Consultants and contractors	2,260,139	–	2,260,139
Provision for (recovery of) loan losses	(3,944,526)	(23,188)	(3,967,714)
Other	(42,598)	–	(42,598)
Depreciation	167,382	–	167,382
U.S. Domestic Program	–	229,059	229,059
Total operating expenses	8,447,900	205,871	8,653,771
Net operating income (loss)	28,534,343	(192,121)	28,342,222
Non-interest income and non-operating expenses			
Gains on sales and call of securities	3,616,047	–	3,616,047
Income (expense) from hedging activities, net	(1,266,924)	–	(1,266,924)
Income (expense) from foreign exchange activities, net	126,332	–	126,332
Fees and other income	680,696	–	680,696
Total non-interest income	3,156,151	–	3,156,151
Income (loss) before program activities	31,690,494	(192,121)	31,498,373
Program activities:			
BEIF:			
EPA grant income	799,248	–	799,248
EPA grant administration	(799,248)	–	(799,248)
CAP expense	(1,178,056)	–	(1,178,056)
WCIF expense	(203,901)	–	(203,901)
Technical Assistance Program:			
EPA grant income	360,698	–	360,698
EPA grant administration	(113,003)	–	(113,003)
IDB-MIF grant income	16,808	–	16,808
Technical assistance program expense	(1,046,005)	–	(1,046,005)
Net program expenses	(2,163,459)	–	(2,163,459)
Income (loss) before non-controlling interest	29,527,035	(192,121)	29,334,914
Net loss attributable to non-controlling interest	(146)	–	(146)
Net income (loss)	$ 29,527,181	$ (192,121)	$ 29,335,060
General Reserve, January 1, 2017			
Allocated paid-in capital	$ –	$ 2,460,790	$ 2,460,790
Retained earnings	173,060,635	(1,668,418)	171,392,217
Current period activity:			
Net income (loss)	29,527,181	(192,121)	29,335,060
Transfer-in from BECC	4,955,236	–	4,955,236
TGP disbursements of the U.S. Domestic Program	–	(121,893)	(121,893)
General Reserve, December 31, 2017			
Allocated paid-in capital	–	2,338,897	2,338,897
Retained earnings	207,543,052	(1,860,539)	205,682,513
	$ 207,543,052	$ 478,358	$ 208,021,410

Note A – The Mexican Domestic Program funds were fully transferred to Mexico as of June 1999.

COMBINING STATEMENT OF COMPREHENSIVE INCOME BY PROGRAM

YEAR ENDED DECEMBER 31, 2017

	International Program	U.S. Domestic Program (A)	Total
Income (loss) before non-controlling interest	$ 29,527,035	$ (192,121)	$ 29,334,914
Net loss attributable to non-controlling interest	(146)	–	(146)
Net income (loss)	29,527,181	(192,121)	29,335,060
Other comprehensive income (loss):			
Available-for-sale investment securities:			
Change in unrealized gain during the period, net	(1,806,949)	–	(1,806,949)
Reclassification adjustment for net gain included in net income	(68,908)	–	(68,908)
Total unrealized loss on available-for-sale investment securities	(1,875,857)	–	(1,875,857)
Foreign currency translation adjustment	(39,664)	–	(39,664)
Unrealized gains (losses) on hedging activities:			
Foreign currency translation adjustment, net	9,029,818	–	9,029,818
Fair value of cross-currency interest rate swaps, net	(11,315,131)	–	(11,315,131)
Total unrealized loss on hedging activities	(2,285,313)	–	(2,285,313)
Total other comprehensive income (loss)	(4,200,834)	–	(4,200,834)
Total comprehensive income (loss)	$ 25,326,347	$ (192,121)	$ 25,134,226

Note A – The Mexican Domestic Program funds were fully transferred to Mexico as of June 1999.

COMBINING STATEMENT OF CASH FLOWS BY PROGRAM

YEAR ENDED DECEMBER 31, 2017

	International Program	U.S. Domestic Program (A)	Total
Operating activities			
Net income (loss)	$ 29,527,181	$ (192,121)	$ 29,335,060
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Depreciation	167,382	–	167,382
Amortization of net premium (discount) on investments	(363,450)	–	(363,450)
Change in fair value of swaps, hedged items and other non-cash items	(14,852,582)	–	(14,852,582)
Non-controlling interest	(146)	–	(146)
Gains on sales and call of securities, net	(3,616,047)	–	(3,616,047)
Provision for (recovery of) loan losses	(3,944,526)	(23,188)	(3,967,714)
Change in other assets and liabilities:			
Increase in interest receivable	(1,974,768)	(34)	(1,974,802)
Decrease in receivable and other assets	2,669,963	–	2,669,963
Decrease in due from U.S. Domestic Program and decrease due to International Program	5,309	(5,309)	–
Decrease in accounts payable	(705,333)	(1,648)	(706,981)
Increase in accrued liabilities	932,511	11,831	944,342
Increase in accrued interest payable	5,103,700	–	5,103,700
Net cash provided by (used in) operating activities	12,949,194	(210,469)	12,738,725
Lending, investing, and development activities			
Capital expenditures	(26,695)	–	(26,695)
Loan principal repayments	218,914,748	329,827	219,244,575
Loan disbursements	(101,425,657)	–	(101,425,657)
Purchase of held-to-maturity investments	(1,011,000)	–	(1,011,000)
Purchase of available-for-sale investments	(694,367,608)	–	(694,367,608)
Proceeds from maturities and call of held-to-maturity investments	54,457,031	–	54,457,031
Proceeds from sales and maturities of available-for-sale investments	212,183,024	–	212,183,024
Net cash provided by (used in) lending, investing, and development activities	(311,276,157)	329,827	(310,946,330)
Financing activities			
Proceeds from other borrowings	13,309,017	–	13,309,017
Proceeds from note issuances	297,891,683	–	297,891,683
Principal repayment of other borrowings	(5,262,000)	–	(5,262,000)
Transfer of funds from BECC	4,955,236	–	4,955,236
Grant funds – EPA	11,903,429	–	11,903,429
Grant disbursements – EPA	(11,908,755)	–	(11,908,755)
Grant activity – U.S. Domestic Program	–	(121,893)	(121,893)
Net cash provided by (used in) financing activities	310,888,610	(121,893)	310,766,717
Net increase (decrease) in cash and cash equivalents	12,561,647	(2,535)	12,559,112
Cash and cash equivalents at January 1, 2017	151,213,774	513,695	151,727,469
Cash and cash equivalents at December 31, 2017	$ 163,775,421	$ 511,160	$ 164,286,581

Note A – The Mexican Domestic Program funds were fully transferred to Mexico as of June 1999.

STATEMENT OF INCOME OF NADB OFFICE IN JUAREZ, CHIHUAHUA

PERIOD FROM NOVEMBER 10 TO DECEMBER 31, 2017

	EPA				
	PDAP	Border 2020	IDB-MIF	Operation	Total
Income:					
U.S. Environmental Protection Agency					
Project Development Assistance Program (PDAP) grant income	$ 285,490	$ –	$ –	$ –	$ 285,490
U.S.-Mexico Border 2020 Program grant income	–	75,208	–	–	75,208
Inter-American Development Bank (IDB) Multilateral Investment Fund (MIF) grant income	–	–	16,808	–	16,808
Interest income	–	–	–	8,431	8,431
Other income	–	–	–	827	827
Total income	285,490	75,208	16,808	9,258	386,764
Operating expenses:					
Personnel	77,590	11,435	–	513,688	602,713
General and administrative	15,830	8,148	–	60,572	84,550
Consultants	–	–	–	37,599	37,599
Depreciation	–	–	–	3,084	3,084
Total operating expenses	93,420	19,583	–	614,943	727,946
Income (loss) before program activities	192,070	55,625	16,808	(605,685)	(341,182)
Technical Assistance Program expense	192,070	55,625	16,808	46,246	310,749
Net income (loss)	$ –	$ –	$ –	$ (651,931)	$ (651,931)

BORDER ENVIRONMENT INFRASTRUCTURE FUND (BEIF)
AS OF AND FOR THE YEAR ENDED DECEMBER 31, 2017

Balance Sheet

	Region 6	Region 9	Total
Assets			
Cash	$ 501	$ 501	$ 1,002
Total assets	$ 501	$ 501	$ 1,002
Liabilities			
Undisbursed grant funds	$ 501	$ 501	$ 1,002
Total liabilities	$ 501	$ 501	$ 1,002

Statement of Income

	Region 6	Region 9	Total
Income:			
U.S. Environmental Protection Agency grant income	$ 340,272	$ 458,976	$ 799,248
Total income	340,272	458,976	799,248
BEIF operating expenses:			
Personnel	305,157	308,191	613,348
Consultants	9,987	126,063	136,050
General and administrative	13,944	14,231	28,175
Operational travel	11,184	10,491	21,675
Total BEIF operating expenses	340,272	458,976	799,248
Net income	$ –	$ –	$ –

Statement of Cash Flows

	Region 6	Region 9	Total
Operating activities			
Net income	$ –	$ –	$ –
Net cash provided by operating activities	–	–	–
Financing activities			
Grant funds – EPA	7,252,021	4,651,408	11,903,429
Grant disbursements – EPA	(7,254,965)	(4,653,790)	(11,908,755)
Net cash provided by financing activities	(2,944)	(2,382)	(5,326)
Net decrease in cash and cash equivalents	(2,944)	(2,382)	(5,326)
Cash and cash equivalents at January 1, 2017	3,445	2,883	6,328
Cash and cash equivalents at December 31, 2017	$ 501	$ 501	$ 1,002

Region 6: EPA Regional Office located in Dallas, Texas
Region 9: EPA Regional Office located in San Francisco, California

SUMMARY
OF FINANCIAL INDICATORS

NADB FINANCIAL RATIOS
2013-2017 (UNAUDITED)[1]

	2017	2016	2015	2014	2013
RATIOS					
Total equity / loans outstanding[2]	49.0%	42.8%	42.7%	45.8%	51.3%
Gross debt / total equity	235.4%	196.6%	210.5%	195.3%	201.8%
Gross debt / callable capital	63.5%	50.5%	51.9%	46.2%	45.6%
Liquid assets / total assets	44.3%	25.3%	25.3%	23.8%	31.3%
Liquid assets / short-term debt	3.12x	87.00x	85.73x	147.96x	-
Non-accrual loans / loans outstanding[2]	1.1%	0.0%	0.0%	0.3%	0.7%
CREDIT RATINGS					
Moody's Investor Service	Aa1/P-1	Aa1/P-1	Aa1/P-1	Aa1/P-1	Aaa/P-1
FitchRatings	AA/F1+	AA/F1+	AA/F1+	AA/F1+	AA/F1+

[1] Excludes the U.S. Domestic Program (see Note 8 of the consolidated financial statements).
[2] Before allowance for loan losses, unamortized fees, and effect of foreign exchange adjustments and hedged items.

CREDITS

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Page 23 (Left, bottom left, middle and top right): Courstesy of Border 2020 Program;
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