Two thousand thirteen

Annual Report

North American Development Bank

Contents

Message from Management

April 2014

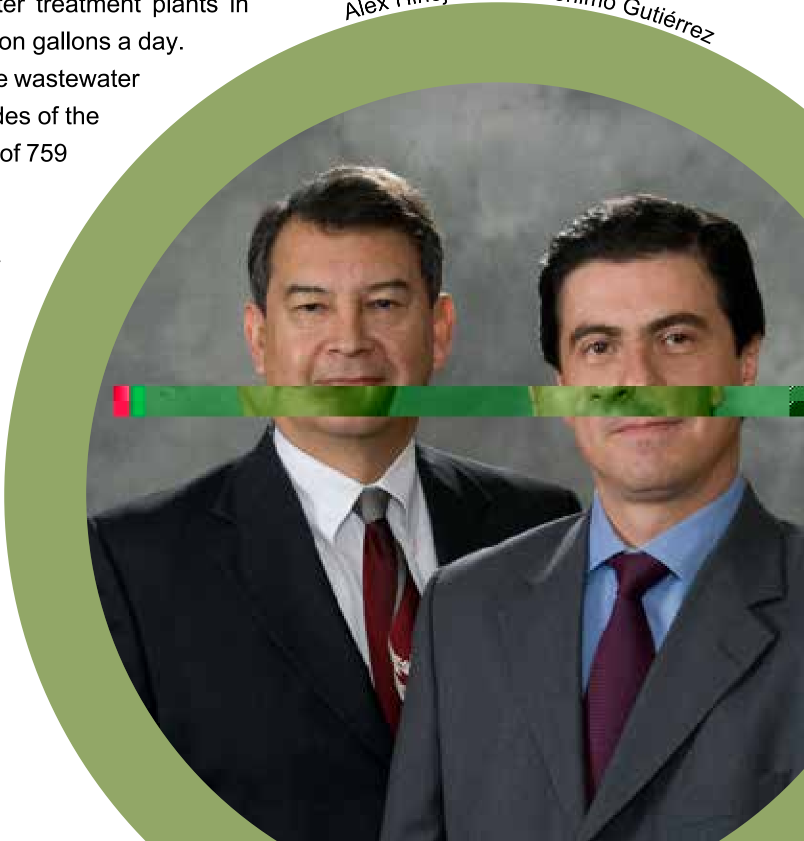
As the **North American Development Bank (NADB)** celebrates its 20th anniversary, its impact on infrastructure in the U.S.-Mexico border region is greater than ever. While maintaining a strong commitment to improving basic infrastructure in the sectors of water, wastewater and solid waste, in 2013 the Bank continued to grow its involvement in the development and financing of other environmental sectors, particularly in the area of clean and renewable energy. Furthermore, along with its sister institution, the Border Environment Cooperation Commission (BECC), and other partner institutions, NADB continued its commitment to strengthen institutional capacities at the state and local level.

Over the past year, the Board of Directors certified 19 new projects with the approval of US$281.53 million in NADB loan and grant financing. Nine of these projects fell within the clean energy sector, including the Bank's first landfill gas-to-energy project, as well as its first transboundary project in which wind energy generated in Mexico will be exported for consumption in the United States. Eight of the remaining projects were in the water sector, including the first five projects to receive grant funding through the Bank's Community Assistance Program (CAP), reflecting the Bank's commitment to support critical environmental infrastructure projects in low-income communities with limited or no capacity to incur debt.

During the same period, the Bank signed financing agreements worth an estimated US$359.72 million with the sponsors of 21 projects and disbursed loans and grants totaling US$232.88 million for the execution of 28 projects. With the majority of this financing in the form of loans, the Bank's outstanding loan balance surpassed the billion dollar mark by year-end.

With respect to project implementation, 17 certified projects receiving financing from NADB initiated construction during the year, while 12 projects were completed and went into operation. Among the projects completed were six solar energy parks and a wind farm in the United States with a combined generation capacity of almost 310 MW, as well as two wastewater treatment plants in Mexico, with a combined treatment capacity of 6.39 million gallons a day. In its 20 years of operation, the Bank has helped increase wastewater treatment capacity by more than 275 mgd along both sides of the border, and more recently has supported the installation of 759 MW of renewable energy generation capacity.

NADB continues to follow a strategy governed by prudent administration of finances and a conservative approach to risk, especially in light of the strong growth of its lending operations with private-sector entities over the past few years. In that context, the Bank implemented additional policy changes in 2013 aimed at further strengthening its financial position, including establishing a debt limit policy and redefining its single obligor limit. Moreover, the Bank engaged a consultant to perform a comprehensive operational risk assessment, which is expected to be


Alex Hinojosa & Gerónimo Gutiérrez

completed in May 2014. Based on the study results, management will take additional steps to improve and strengthen its operational processes and procedures.

At the governance level, the United States and Mexico continue to demonstrate strong shareholder support for NADB. In September 2013, the two governments launched a high level economic dialogue (HLED) in order to advance strategic economic and commercial priorities central to promoting mutual economic growth, job creation, and global competitiveness. Within this framework, the two governments recognized the importance of making effective and efficient use of the Bank in developing cooperative efforts related to the HLED. In this context, the Board of Directors adopted a resolution in November 2013 directing the Bank to support the two governments in mapping priority port-of-entry infrastructure projects and identifying potential financing structures for them, as well as defining benchmarks for aligning the port-of entry development process between the two nations.

At 20 years of operation, NADB has evolved into an institution that has had a transformative impact on the quality of life for residents in the border region through the development and financing of infrastructure that preserves, protects and enhances the environment. The Bank has contracted financing for 192 projects throughout the 10-state border region, providing US$2.25 billion in loan and grant financing. The total investment value of these projects exceeds US$5.66 billion, demonstrating the leveraging effect of the NADB-BECC project development process.

Going forward, Bank management is focused on a strategy to continue strengthening NADB and its ability to serve the needs of border communities. These efforts include maintaining a conservative approach with respect to credit and market risk, liquidity and asset-liability management; diversifying its sources of funding; and identifying new sectors of infrastructure within the Bank's mandate for project diversification.

As always, we would like to take this opportunity to thank all of our partners in both countries whose support has been instrumental in helping NADB carry out its mission, as well as evolve into a mature financial institution with both the tools and experience to address the needs of the border. We look forward to working with you in making the coming years even more rewarding.

We are proud to present to you the 2013 North American Development Bank Annual Report.

Gerónimo Gutiérrez
Managing Director

Alex Hinojosa
Deputy Managing Director

2013 in a Snapshot

Project Activity

During the course of the year, 12 projects completed construction and went into operation, including six solar energy plants and one wind farm that represent almost 310 megawatts of installed power generation capacity from renewable resources, as well as four wastewater projects, which altogether increased wastewater treatment capacity by 6.39 million gallons a day (mgd) and expanded sewer systems to collect an estimated 2.5 mgd of wastewater. Expansion of the water distribution system in Colonia Esperanza, Chihuahua, was also completed, increasing service coverage from about 50% to 100% of the community.

Eleven additional projects in various sectors began construction, including a 57-mgd wastewater treatment plant in Hermosillo, Sonora, partially funded with a NADB loan, and a water transmission line in San Luis, Arizona, the first project to be funded with a CAP grant.

First wastewater treatment plant begins operation in Nogales, Sonora

In February 2013, the Los Alisos Wastewater Treatment Plant and conveyance system began operations in Nogales, Sonora. The new plant, which has the capacity to treat up to 5.02 mgd of wastewater, is the first in this city of 214,000 residents. Previously, all the wastewater collected in Nogales, Sonora, was conveyed to the Nogales International Wastewater Treatment Plant (NIWWTP) located in Rio Rico, Arizona. However, in recent years, wastewater flows from Nogales have increased in volume due to population growth and expanded collection coverage. The new plant is eliminating the excess wastewater flows going to the NIWWTP, as well as treating additional wastewater flows that were being discharged untreated into the Santa Cruz River basin.

The US$19.3 million project was certified by BECC in 2010 and was financed by an US$8.0 million grant through the Border Environment Infrastructure Fund (BEIF), a US$3.3 million NADB loan and US$8.0 million from the Mexican federal and state governments.

Six solar parks begin clean power production in U.S. border states

Six of the eight solar parks that began construction in 2013 were completed and in operation by the end of the year. These six parks—five located in California and one in Texas—have a combined generation capacity of 44.5 megawatts and together are expected to displace an estimated 40,432 metric tons of carbon dioxide a year, which according to the Greenhouse Gas Equivalencies Calculator of the U.S. Environmental Protection Agency would be the same as removing 8,512 passenger vehicles from the road.

These projects certified by BECC in 2012 and 2013 represent a total investment of US$189.3 million, including loans from NADB for US$122.4 million.

El Centro Solar Park in California

Third wastewater project completed in San Luis Rio Colorado, Sonora

Expansion of the wastewater system to unserved areas south of the city was completed in September 2013, extending access to sewer services to approximately 85% of the city. The project was the third phase of a comprehensive wastewater infrastructure improvements plan initiated by the local water utility in 2000. At that time, less than half of the population had sewer service, and the wastewater collected was discharged untreated into a dry bed of the Colorado River. The first phase, which consisted of improving the wastewater collection and conveyance systems and constructing the first two treatment modules of the Las Palmas Wastewater Treatment Plant, was completed and began operations in the first half of 2007. Under the second phase, which was completed at the end of 2010, the wastewater collection system was expanded and the treatment capacity of the plant was increased from 9 mgd to 13.7 mgd. Today, approximately 63% of the wastewater generated by city is being collected and treated prior to discharge.

Altogether, these projects represent a total investment of US$37.9 million, and were funded with US$9.0 million in loans from NADB, US$14.7 million in BEIF grants and US$14.2 million from Mexican federal, state and local sources. The next phase to continue expansion of the wastewater collection system is already in development and expected to be certified in early 2014.

Lending Activity

As a result of 2013 activity, the Bank's outstanding loan balance grew to US$1.01 billion by the end of the year. Eleven new loan commitments totaling US$273.24 million were approved by the Board of Directors, including funding for the first landfill gas-to-energy project. Eight of those loan commitments were contracted before year-end, along with three commitments approved the previous year. In total, the Bank signed 11 loan agreements for US$349.88 million. A breakdown of the loans approved and contracted by sector during 2013 is shown in Tables 1 and 2, respectively.

While renewable energy projects continued to be a central part of the Bank's financing activity in 2013—with US$170 million contracted for seven solar energy projects—more than half of the loan funds contracted were committed to projects in other sectors, including the first desalinization plant funded by the Bank.

Eight of the eleven loans contracted during the year were partially or fully disbursed by year-end for a total of US$135.12 million. Altogether for the year, NADB disbursed US$214.96 million in loans for the implementation of 15 certified projects. During the same period, the Bank received a total of US$73.73 million in principal payments, including the final payment of the first loan contracted by the water utility in Tecate, Baja California to expand and improve its water and sewer systems, as well as the prepayment of three loans contracted by the Municipality of Nogales, Sonora, to purchase solid waste equipment and improve air quality through street paving.

TABLE 1
New Loan Commitments Approved in 2013
(US$ Millions)

Sector	No.	Amount
Air quality - road improvements	1	$ 8.60
Basic urban infrastructure*	1	19.10
Landfill gas-to-energy	1	3.07
Solar energy	7	192.47
Wind energy	1	50.00
Total	**11**	**$ 273.24**

TABLE 2
New Loan Commitments Signed in 2013
(US$ Millions)

Sector	No.	Amount
Air quality - road improvements	2	$ 136.53
Basic urban infrastructure*	1	19.10
Solar energy	7	169.99
Water	1	24.26
Total	**11**	**$ 349.88**

* These projects consist of a mix of works from different sectors, such as water, wastewater, storm drainage and roadway improvements.

Electric substation in Ocotillo, CA

Lift station in Brawley, CA

Grant Activity

With the approval of the Board of Directors, NADB uses a limited portion of its retained earnings to finance grant programs to help make municipal infrastructure projects more affordable for border communities. Having closed out the Solid Waste Environmental Program (SWEP) at the end of 2012, NADB had two grant financing programs in 2013: the Community Assistance Program (CAP) and the Water Conservation Investment Fund (WCIF).

Along with these programs, NADB also administers grant funding provided by the U.S. Environmental Protection Agency (EPA) for the implementation of high-priority public drinking water and wastewater infrastructure projects. These funds, which are channeled through the Border Environment Infrastructure Fund (BEIF), have been key to increasing wastewater collection and treatment along both sides of the U.S.-Mexico border.

Community Assistance Program (CAP)

In February 2011, the Board approved the creation of the CAP program to provide grant financing for the implementation of critical environmental infrastructure projects in low-income communities where debt is not a viable option. Grants are available for public-sector projects in all environmental sectors eligible for NADB financing, with priority given to drinking water, wastewater, water conservation and solid waste infrastructure. In December 2013, the CAP guidelines were revised to eliminate specific application periods, thereby allowing project sponsors to submit applications at any time.

During 2013, NADB approved and contracted US$2.18 million in CAP grants to support the implementation of five infrastructure projects, which are listed in Table 3. In addition, a small portion of CAP funding is being used to cover the construction supervision costs of these projects. Table 4 provides a summary of CAP funding activity in 2013, as well as the overall status of the program at year-end.

TABLE 3
CAP Grants Approved and Contracted in 2013
(US$ Millions)

Community Benefitted	Project Type	Amount	Date Approved	Date Contracted
San Luis, AZ	W	$ 0.50	13-Mar-13	11-Jul-13
Brawley, CA	WW	0.45	13-Mar-13	23-Aug-13
Santiago, NL	SD	0.33	9-May-13	3-Jul-13
Sunland Park, NM	W	0.45	9-May-13	24-Sep-13
Nuevo Casas Grandes, CHIH	WW	0.45	22-Jul-13	13-Sep-13
		$ 2.18		

SD = Storm drainage; W = Water; WW = Wastewater

TABLE 4
Annual and Cumulative CAP Financing Activity
(US$ Millions)

	2013	Cumulative
Retained earnings allocated*	$ 1.06	$ 11.47
Funds used for supervision	0.17	0.17
Grant approvals	2.18	2.18
Grants contracted	2.18	2.18
Disbursements to projects	-	-
Contracted grants, not yet disbursed		$ 2.18
Additional approvals, not yet contracted		-
Funding available for future projects		9.12

*2013 allocation is the unused funds rolled over from the WCIF.

Prior to the end of the year, construction began on the water transmission main to interconnect the two water distribution systems in San Luis, Arizona. The remaining four projects were either in bidding or under final development.

Water Conservation Investment Fund (WCIF)

In August 2002, the Board of Directors created this program to address an urgent need for water conservation financing in the border region, and made a one-time allocation of US$80.00 million from the Bank's retained earnings to fund the program.

During 2013, the Bank disbursed US$0.45 million in WCIF funds for implementation of one project and closed out the financing agreements of two completed projects resulting in the deobligation of US$0.95 million in unused WCIF funds. At the end of 2013, the Bank had US$3.82 million in contracted WCIF funds pending disbursement for four projects in Texas, which were in various stages of development.

BOX 1
Program Results

No. of projects funded	23
Total project investment	US$232.4 million
Total WCIF grants	US$78.9 million
Leveraging	Almost 3:1
Total estimated water savings	371,672 acre-feet a year

Since almost all of the WCIF funds had been committed to specific projects by the end of 2012 and water conservation projects may be financed through the CAP as a priority sector, in May 2013, the Board agreed to discontinue the WCIF and roll any uncommitted or unused funds over to the CAP. As a result, a total of US$1.06 million in uncommitted WCIF funds was transferred to the CAP program in 2013. Once the last four projects have been completed, the WCIF program will be fully closed out and any unused funds from those projects will also be rolled over to the CAP.

Border Environment Infrastructure Fund (BEIF)

BEIF grants, which are fully funded by EPA, target public drinking water and wastewater infrastructure projects within 100 km of both sides of the U.S.-Mexico border. In the case of Mexican projects, BEIF funding is matched dollar for dollar by Mexican grants, mainly through the federal water agency, *Comisión Nacional del Agua* (CONAGUA), which also plays an important role in the authorization of those projects.

In 2013, EPA approved grants totaling US$6.10 million for three wastewater collection projects in Arizona and California. During the same period, NADB contracted five BEIF grants totaling US$7.66 million with the respective project sponsors, including the three grants approved during the year. As a result, all approved BEIF grants were contracted by year-end. Details about the grants contracted during the year are provided in Table 5.

TABLE 5
BEIF Grants Contracted in 2013
(US$ Millions)

Community Benefitted	Project Type	Amount	Date Certified	Date Contracted
Bisbee, AZ (Tintown)	WW	$ 0.76	8-Nov-12	6-Mar-13
Sierra Vista, AZ	WW	3.97	30-Apr-13	7-Jun-13
San Agustin, CHIH	W / WW	0.79	8-Nov-12	13-Jun-13
Holtville, CA	WW	1.89	9-May-13	9-Oct-13
Holtville, CA	WW	0.25	9-May-13	9-Oct-13
		$ 7.66		

W = Water; WW = Wastewater

Altogether, these five projects are expected to help eliminate an estimated 1 mgd of untreated or inadequately treated wastewater.


Sierra Vista, AZ


Holtville, CA


Rio Grande City, TX

A total of US$17.46 million in BEIF funds was disbursed for the implementation of 13 projects during the course of 2013, leaving a balance of approximately US$28.44 million pending disbursement at year-end. Table 6 provides a summary of BEIF funding activity in 2013, as well as the overall status of the program since inception.

TABLE 6
Annual and Cumulative BEIF Financing Activity
(US$ Millions)

	2013	Cumulative
EPA funding allocations*	$ 3.67	$ 647.19
Grant approvals	6.10	597.70
Grants contracted	7.66	597.70
Disbursements to projects	17.46	569.26
Cancellations**	(1.11)	(54.93)
Contracted grants, not yet disbursed		$ 28.44
Additional approvals, not yet contracted		-
Funding available for projects in development		49.49

* Amount allocated for project construction; does not include funds set aside for administration expenses.

** Unused funds deobligated from completed projects and returned to the BEIF program for projects in development.

Four wastewater projects and one drinking water project completed construction during 2013. These projects include, in addition to those highlighted on pages 3 & 5, upgrading the treatment process and doubling the capacity of the Rosarito I Wastewater Treatment Plant from 1.37 to 2.74 mgd in Playas de Rosarito, Baja California, and providing first-time wastewater collection service to 27 households on Water Street in Rio Grande City, Texas.

Rosarito I Wastewater Treatment Plant

Technical Assistance & Training

In addition to financing for project implementation, NADB also uses a small allocation of its retained earnings to provide technical assistance and training to project sponsors to strengthen their financial performance and ensure the long-term sustainability of their infrastructure. Through the Technical Assistance Program (TAP), grants are provided to help finance studies related to the planning and design of environmental infrastructure works, as well as for capacity-building measures aimed at achieving the effective and efficient operation of public services. Through the Utility Management Institute (UMI), NADB offers an annual series of seminars on the financial administration and planning of water utilities, both at its headquarters in San Antonio, Texas, as well as on site to regional groups.

In 2013, technical assistance grants totaling US$568,000 were approved for five project development studies or activities (see Box 2). During the course of the year, three projects were also completed with TAP grants totaling US$388,000, including the first two projects shown in Box 2, as well as a pilot solar energy capacity-building project for the Chihuahua state government involving the installation of a solar plant to supply electricity to the new children's hospital in the city of Chihuahua, which helped cut its energy costs by about 15 percent in the first year of operation. At the close of 2013, technical assistance grants totaling US$509,535 were committed to the development of four studies currently in process.

BOX 2
TAP Grant Approvals in 2013

- Preliminary designs for the Bahía de Kino and La Victoria/Tazajal wastewater treatment plants in Hermosillo, Sonora
- Study of renewable energy tax incentives in Mexico
- Pilot solar energy capacity-building project for the Las Californias Children's Hospital in Tijuana, Baja California
- Study to identify and implement solutions for closure of the open-air dumpsite in San Luis Rio Colorado, Sonora
- Border-wide analysis of international ports of entry


Children's hospital in Chihuahua, CHIH


Dumpsite in San Luis Rio Colorado, SON


Las Californias Children's Hospital, Tijuana, BC

With respect to training, UMI concluded its 14th year of seminars in 2013, training a total of 277 utility personnel through various programs. Its four-module basic management program was presented to 50 utility administrators from 22 border communities in the U.S. and Mexico, including a regional group co-sponsored by the Sonora state water agency, *Comisión Estatal de Agua de Sonora* (CEAS) in Hermosillo, Sonora. In addition, an in-depth seminar on how to successfully implement water rates was presented to two regional groups in Mexico. The first session was co-sponsored by the local utility, *Comisión Estatal de Servicios Públicos de Mexicali* (CESPM), in Mexicali, Baja California, and was attended by 47 utility professionals, including representatives from the neighboring utility in San Luis Rio Colorado, Sonora. The second session sponsored by CEAS in Hermosillo, Sonora, was presented to 26 utility professionals from 19 communities in that state. The seminar covered developing a cost-based rate index and adequate rate structuring, as well as communication and negotiation strategies for gaining public acceptance of new rates.

TABLE 7
Wastewater Treatment Plant Training in Mexico in 2013

Community	Utility	No. of participants
Tecate, B.C.	CESPTe	32
Playas de Rosarito, B.C.	CESPT	29
San Luis Rio Colorado, SON	OOMAPAS	18
Sonoyta, SON	OOMAPAS	23
Juarez, CHIH	JMAS	17
Reynosa, TAMPS	COMAPA	24
Hermosillo, SON	CEA	11

NADB also extended the training program for Mexican wastewater treatment plant operators developed in collaboration with EPA and the Latin American and Caribbean water center, *Centro del Agua para América Latina y el Caribe* (CDA), of the Monterrey Technological Institute (ITESM). As shown in Table 7, a total of 154 wastewater operators from seven utilities received both classroom instruction and hands-on training in the adequate and efficient operation and maintenance of wastewater treatment plants so as to facilitate compliance with current effluent quality standards.

Lab analysis in Reynosa, TAMPS

TABLE 8

FINANCIAL SUMMARY 2013-2009[1]

(US$ Thousands)

	2013	2012	2011	2010	2009
Operational Highlights					
Loan commitments signed	$ 349,881	$ 559,120	$ 105,908	$ 129,014	$ 211,900
Loan disbursements	214,964	501,500	80,347	171,796	134,824
Loan repayments	73,733	52,753	122,811	12,141	10,678
Undisbursed portion of committed loans	238,780	119,819	62,199	44,903	102,923
Balance Sheet Data					
Cash and cash equivalents	$ 56,810	$ 62,357	$ 36,778	$ 38,403	$ 34,283
Investments	488,715	326,217	313,791	236,040	135,912
Loans outstanding, net[2]	961,507	859,714	388,241	457,314	282,501
Total assets	1,573,076	1,302,304	820,018	754,399	490,616
Borrowings outstanding, gross	1,046,386	730,000	250,000	250,000	-
Total liabilities	1,054,422	780,457	286,822	261,421	1,130
Total equity	518,654	521,848	533,197	492,978	489,486
Callable capital	2,295,000	2,295,000	2,295,000	2,295,000	2,295,000
Income Statement Data					
Loan income	$ 35,149	$ 19,344	$ 20,994	$ 20,512	$ 11,384
Investment income	4,386	7,779	6,907	11,400	11,883
Other income	46	590	9,420	529	602
Operating expenses	20,377	11,407	10,397	8,733	7,844
Administrative expenses[3]	8,871	8,425	7,999	6,768	6,517
Provision for loan losses	10,544	-	2,350	900	800
Other expenses	962	2,982	48	1,065	527
Interest expense	10,838	5,363	4,532	4,095	-
Litigation expense	-	1,484	-	-	-
Income before grant program activity	8,366	9,458	22,392	19,613	16,024
Program expenses[4]	1,145	2,437	737	2,121	5,698
Net income	7,221	7,020	21,655	17,492	10,326
Ratios					
Adjusted shareholders' equity[5] / loans outstanding, net	51.8%	58.2%	131.3%	104.1%	166.6%
Gross debt / callable capital	45.6%	31.8%	10.9%	10.9%	-
Gross debt / adjusted shareholders' equity	210.1%	145.8%	49.0%	52.5%	-
Interest coverage[6]	2.8x	3.6x	6.5x	6.3x	-
Liquid assets / total assets	31.3%	25.7%	36.3%	29.3%	33.9%
Operating income / adjusted shareholders' equity	1.7%	1.9%	4.4%	4.1%	3.4%
Operating income / average assets	0.6%	0.9%	2.8%	3.2%	6.5%

[1] Excludes the U.S. domestic program (see page 23).

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

[3] Administrative expenses is defined as the sum of personnel, consultants, operational travel and general and administrative.

[4] Program expenses include grant financing and technical assistance funded from the Bank's retained earnings, but excludes the Border Environment Infrastructure Fund (BEIF), which is fully funded by the U.S. Environmental Protection Agency.

[5] Adjusted shareholder' equity is defined as the sum of undesignated paid-in capital, undesignated retained earnings, reserves, and accumulated other comprehensive income.

[6] Interest coverage ratio is defined as total revenue minus administrative expenses divided by interest expense.

Mandate & Governance

NADB is a binational financial institution established by the governments of the United States and Mexico for the purpose of financing environmental infrastructure projects in the U.S.-Mexico border region (the “international program”) and community adjustment and investment projects throughout the U.S. and Mexico in support of the purposes of the North American Free Trade Agreement (NAFTA) (the “domestic programs”). The scope of the Bank’s mandate—including the geographic jurisdiction and environmental sectors in which it may operate—as well as its functions and limitations, are defined in an agreement between the two governments (the “Charter”).

Under the international program, NADB is charged with providing financing to public and private entities for environmental infrastructure projects certified by its sister organization, BECC, as well as offering technical and other assistance to support the development and implementation of eligible projects.

Eligible Environmental Sectors

◆ **Water** Potable water supply, wastewater treatment and reuse, water conservation, storm drainage	◆ **Air quality** Street paving, roadway improvements, ports of entry, public transportation, methane capture, industrial emissions
◆ **Waste management** Sanitary landfills, collection & disposal equipment, dumpsite closure, recycling	◆ **Industrial / hazardous waste** Treatment & disposal facilities, industrial site remediation
◆ **Cleaner / renewable energy** Solar, wind, biogas, biofuels, hydroelectric, geothermal	◆ **Energy efficiency** Industrial equipment retrofits, public lighting & building upgrades

As defined in the Charter, projects that qualify as environmental infrastructure under the international program 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 international boundary in the four U.S. states of Texas, New Mexico, Arizona and California and within 300 kilometers (about 186 miles) south of the border in the six Mexican states of Tamaulipas, Nuevo Leon, Coahuila, Chihuahua, Sonora, and Baja California. However, projects beyond these areas may be deemed eligible if the Board determines that they remedy a transboundary environmental or health problem.

Pursuant to the Charter, NADB and BECC are 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 the Bank’s programs and financing proposals involving NADB funds.

Board of Directors

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
Mexican border state representative	U.S. border state representative
Mexican border resident representative	U.S. border resident representative

* Board chair, 2013

Under the domestic programs, the two governments allocated ten percent of the Bank’s equity to establish a program in each country and, at the request of the U.S. government, the Bank continues to administer the funds of the U.S. domestic program, which is operated completely independently of the international program (see Domestic Programs under Business Operations). Unless otherwise specified, the information contained in this report pertains solely to the Bank’s international program.

Management Discussion & Analysis

New Developments

Given the strong growth of its lending operations with private-sector entities in the past couple of years, NADB adopted several policies and took other actions in 2013 to further mitigate its exposure to risk and strengthen its financial position.

Single Obligor Limit: In May 2013, NADB amended its Loan Policies and Procedures to redefine the formula used to calculate the single obligor limit (SOL). Under the old formula, the SOL was calculated as a percentage of the Bank's "available capital resources," which was defined as funded, unimpaired paid-in capital, plus undesignated retained earnings, plus eligible callable capital, where "eligible callable capital" was defined as callable capital that corresponds to current borrowing by the Bank. Consequently, as the Bank began regular borrowings in the capital markets to support its growing loan portfolio, the SOL also increased significantly.

Under the new formula, the SOL is calculated as a percentage of the Bank's "usable equity," which is defined as funded, unimpaired paid-in capital, plus undesignated retained earnings, plus the Special Reserve, plus the Capital Preservation Reserve. The new formula, which is consistent with sound credit risk management practices in the international banking industry, provides a more stable SOL that will increase or decrease based on available reserves and NADB's capacity to absorb unexpected losses. With US$478.3 million in usable equity at the close of 2013, the SOL was US$95.66 million and up to US$143.49 million for obligors that met certain risk-related criteria.

Debt Limit Policy: Although the Charter does not establish an explicit limit on what the Bank can borrow to support its loan portfolio and liquidity requirements, there is an implicit limit deriving from the amount that the Bank can lend. To provide greater clarity on the Bank's borrowing limit and to formalize the commitment of Bank management to oversee leverage levels, NADB established a debt limit policy in May 2013. Under the new policy, the Bank's total principal outstanding debt may not exceed at any time the callable portion of its subscribed capital shares associated with the international program, plus the minimum liquidity level required by the Bank's liquidity policy. In addition, Bank management must inform the Board when reasonable estimates indicate that the outstanding debt will reach 80% of subscribed callable capital within the following six-month time period. The new policy is fully compatible with the Bank's lending limit under the Charter.

Program Terminations: In May 2013, the Board of Directors approved the termination of a grant program and concessional lending facility that had fulfilled their purposes.

In November 2000, NADB was authorized to offer below-market interest rate lending on a limited basis for public projects in the water and solid waste sectors in order to boost its lending operations by making its loans more accessible to border communities. The Low Interest Rate Lending Facility (LIRF) was established in 2001 and funded with up to US$100 million in paid-in capital, of which US$76.2 million was used to make loans. Given prevailing low market rates in recent years, border communities are able to access Bank financing at its ordinary, market-related rates, and no LIRF loan has been made since 2007. Therefore, the Board agreed to terminate the LIRF. At the close of 2013, LIRF loans accounted for 5.0% (US$50.35 million) of the Bank's outstanding portfolio.

The Board created the Water Conservation Investment Fund (WCIF) in August 2002 to address an urgent need for water conservation financing in the border region, and made a one-time allocation of US$80.00 million from the Bank's retained earnings to fund the program. At the close of 2012, 99.9% of the allocated funding had been committed to specific projects. Since any future water conservation projects may be financed through the CAP created in 2011 to consolidate the Bank's grant financing activity, the Board agreed to discontinue the WCIF and roll any uncommitted or unused funds over to the new program, as long as water conservation projects were included as one of its project priorities.

Special Reserve Policy and General Allowance for Loan Losses: In addition to specific loan loss provisions on non-performing loans, in November 2013, NADB began creating general provisions on loans made to private-sector borrowers based on probabilities of default and expected recovery rates. The general allowance will be maintained at a level considered adequate by management to provide for probable and estimable losses inherent in the loan portfolio and in accordance with generally accepted accounting principles. The provisioning for this allowance is recorded as an expense in the statement of income. For the year ended 2013, general provisions of US$9.45 million were expensed under this policy, corresponding to US$641.97 million in outstanding private-sector loans.

Since the general loan loss allowance and the Special Reserve serve similar purposes, NADB amended its Special Reserve policy to take into account the general loan loss allowance and set a targeted minimum balance of US$30.00 million. With this amendment, the sum of the Special Reserve and general allowance for loan losses will be at least equal to, if not greater than, the Special Reserve as calculated under the previous formula, depending on the risk profile of the loan portfolio. Under the amended policy, the Special Reserve was increased from US$27.30 million in December 2012 to US$30.00 million in December 2013.

Business Operations

Under its international program, the Bank provides loan and grant financing and technical assistance for environmental infrastructure projects, as well as administers grant funding provided by other entities. Prior to financing approval, the technical feasibility and environmental impacts of the projects are evaluated and verified by BECC through a certification process that ensures transparency and promotes public participation. Project certification and financing proposals are approved simultaneously by the Board of Directors. Although project implementation is the responsibility of the project sponsors, NADB provides substantial project oversight and support during the procurement and construction phases of project execution to ensure that the proceeds of its loans and grants are used efficiently and for purposes within the scope of the certified project.

Lending Operations

The Bank's lending operations are designed to ensure that loans are made to financially sound entities and that funds are utilized as intended to implement technically and economically viable projects. To that end, the Bank performs a thorough due-diligence analysis of the technical and financial viability of each project considered for loan financing. In the case of certain borrowers and projects, this in-house analysis is further supported by external advisors who examine and structure the loans from a legal, technical, and financial perspective. The Bank negotiates individual loan agreements based on its policies and the needs of a particular borrower or project. Loan disbursements are made subject to the fulfillment of conditions set forth in each individual loan agreement.

Loans are generally offered at fixed or variable market rates, payable monthly, quarterly or semi-annually and with maturities of up to 25 years. For U.S. borrowers, loans are available in U.S. dollars. For Mexican borrowers, loans are available in Mexican pesos or in U.S. dollars if the project generates a U.S. dollar cash flow. For loans made in Mexican pesos, the Bank's exchange rate risk is fully hedged through cross-currency swaps. Loans are also generally secured by some form of credit support.

Loans may be made to public and private borrowers. In its early years of operation, the vast majority of loans were made to states and local municipalities. In recent years, NADB has worked more with private borrowers due to their heavier involvement in newly addressed sectors such as renewable energy. Consistent with NADB's risk management philosophy, private borrower lending is subject to an even more stringent analysis and credit enhancement requirements. The Bank also supports public-private partnerships as a sound means of financing public infrastructure, especially for water supply and wastewater treatment projects. In most cases these partnerships are implemented through a build-operate-transfer (BOT) agreement, where the private contractor is the borrower and the municipality or utility is the source of payment and/or guarantor.

The Bank may act as sole lender or co-finance projects with other public or private financiers, depending upon the characteristics and financing needs of a project. In its early years, almost all of the Bank's co-financed projects were through a consortium with other governmental lenders, mainly in the wastewater sector. More recently, the Bank has participated in several project finance transactions with a co-financing structure where the Bank will be repaid *pari passu* and share collateral pro-rata with the other lenders. The Bank expects to participate in more co-financing structures of this nature, which will allow it to finance larger projects while limiting its credit exposure.

The Bank funds loans with its equity or borrowed monies. Under its 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 the capital resources of the Bank. As of December 31, 2013, the total unimpaired subscribed capital of the Bank was US$2.70 billion (paid-in capital and callable capital allocated to the international program) and its unimpaired reserves and undesignated retained earnings were US$101.12 million, for a total loan limit of US$2.80 billion, up slightly from US$2.79 billion at the end of 2012.

As a matter of prudent risk management, the Bank also imposes limits per project and per borrower. In general, NADB cannot lend a project more than 85% of eligible project costs. The single obligor limit (SOL) is set at 20% of the Bank's usable equity (funded, unimpaired paid-in capital, plus undesignated retained earnings, the Special Reserve, and the Capital Preservation Reserve), and an additional 10% may be made available for obligors that meet certain risk-related criteria. As of December 31, 2013, the 20% SOL limit was US$95.66 million and the 30% SOL limit was US$143.49 million.

Lending Activity: A five-year summary of the Bank's lending activity is included in Table 8. Over the past five years, new loan commitments have averaged US$271.16 million per year. During 2013, NADB signed 11 loan agreements totaling US$349.88 million, a 37.4% decrease compared to the 11 loans totaling US$559.12 million contracted in 2012. A breakdown of the loans contracted by sector during 2012 and 2013 is shown in Table 9.

During 2013, loan disbursements totaled US$214.96 million, including the partial or full disbursement of eight loans contracted during the year, and represented a 57.1% decrease compared to 2012 (US$501.50 million). Over the past five years disbursements have averaged US$220.69 million.

A breakdown of disbursements by sector during 2012 and 2013 is shown in Table 10. Solar energy loans accounted for more than half of the disbursements (56.8%) in 2013, followed by wind energy loans with 17.4% and water and wastewater loans with 15.7%. More than 74% of the loans disbursed in 2013 went to private-sector borrowers in the U.S. and the remaining 25.8% to public-sector (16.9%) and private-sector (8.9%) borrowers in Mexico. At the end of 2013 an estimated US$238.78 million in contracted loan commitments was pending disbursement, mainly for air quality paving and solar energy projects.

Loan Portfolio: As of December 31, 2013, the Bank's outstanding loan balance came to US$1.01 billion, an increase of 16.2% over the balance at the end of 2012 (US$869.98 million). Figure 1 illustrates the annual growth of the loan portfolio over the past four years. For the period from December 31, 2009 to December 31, 2013, the loan portfolio grew at an average annual rate of 34.3%.

TABLE 9
Loan Commitments Signed
(US$ Millions)

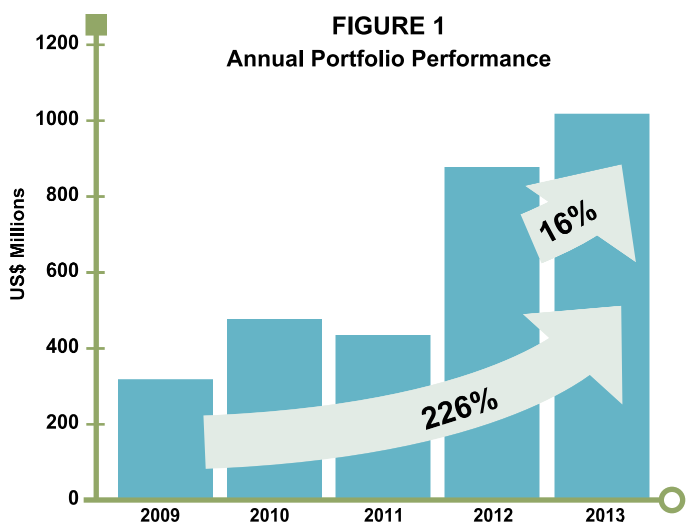
Sector	2013	2012
Air quality	**$ 136.53**	$ 11.02
Basic urban infrastructure*	**19.10**	13.26
Solar energy	**169.99**	107.03
Water /wastewater	**24.26**	46.81
Wind energy	**-**	381.00
Total	**$ 349.88**	$ 559.12

TABLE 10
Loan Disbursements
(US$ Millions)

Sector	2013	2012
Air quality	**$ 10.64**	$ 5.25
Basic urban infrastructure*	**11.08**	17.70
Solar energy	**122.06**	128.07
Water / wastewater	**33.77**	6.89
Wind energy	**37.41**	343.59
Total	**$ 214.96**	$ 501.50

* These projects consist of a mix of works from different sectors, such as water, wastewater, storm drainage and roadway improvements.

FIGURE 1
Annual Portfolio Performance

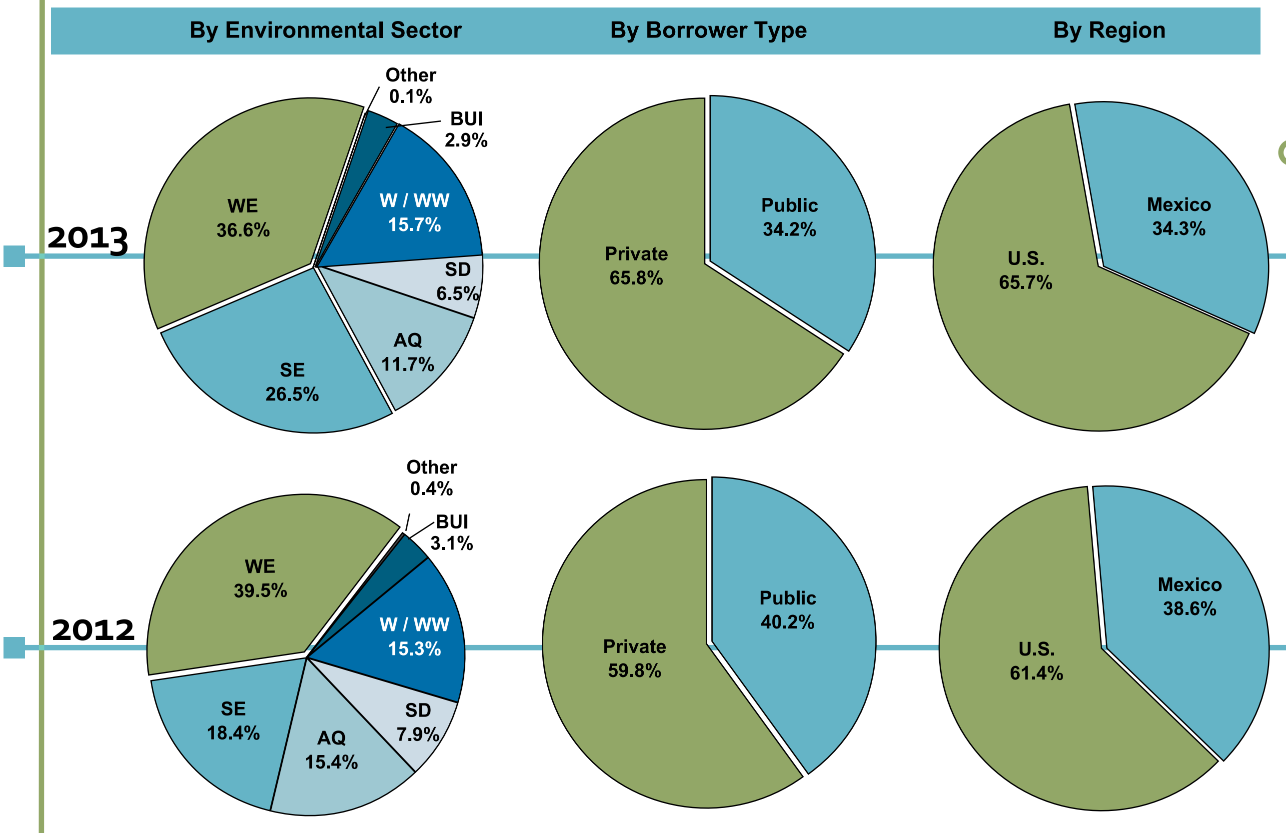


A breakdown of the loan portfolio by environmental sector, borrower type and geographic region for the years ending in 2012 and 2013 is shown in Figure 2.

Changes in the monetary value of loans by environmental sector during the 12-month period ending December 31, 2013 are provided in Table 11. Solar energy loans had the most significant growth, increasing 67.3% from US$159.96 million in 2012 to US$267.62 million in 2013, followed by water and wastewater loans, which grew 19.4% from US$133.04 million to US$158.84 million. Wind

FIGURE 2

Breakdown of Outstanding Loan Balances



* Air Quality (AQ), Basic Urban Infrastructure (BUI), Storm Drainage (SD), Solar Energy (SE), Water/Wastewater (W/WW), Wind Energy (WE)

** Other included solid waste and biofuel in 2012 and biofuel in 2013.

energy and basic urban infrastructure also registered modest growth during 2013, while the remaining sectors declined in varying degrees due to principal payments, which included the prepayment of two air quality loans and the only remaining solid waste loan.

As a result of these changes, wind energy accounted for just over a third (36.6%) of the Bank's loan portfolio at the close of 2013, down slightly from 39.5% in 2012, and was followed by solar energy with 26.5% (compared to 18.4% in 2012) and water and wastewater with 15.7% (compared to 15.3% in 2012). The other sectors remained fairly stable during 2013 (see Figure 2), with the exception of air quality, which declined from 15.4% to 11.7%, mainly due to prepayments.

Given that the border region offers ideal conditions for solar and wind energy projects, the Bank expects to see continued demand for loans in the those sectors. In addition, the Bank continues to pursue environmental projects in other areas, including public transportation. Of the US$238.78 million in contracted loan commitments pending disbursement at the end of the year, 77.2% (US$184.2 million) was for air quality, basic urban infrastructure, water and wastewater projects.

In terms of portfolio distribution by borrower type, the volume of loans held by private-sector borrowers increased 28.0% from US$520.13 million in 2012 to US$665.84 million in 2013, while the balance of outstanding loans held by governmental borrowers dropped slightly from US$349.85 million to US$345.38 million during the same 12-month period.

Portfolio distribution by geographic region basically mirrored the trend of private and public sector loans since all new loans to governmental borrowers went to finance projects in Mexico, and the majority of private-sector loans went to projects located in the Unites States in 2013. As of December 31, 2013, loans invested in U.S. projects accounted for US$664.66 million of the loan portfolio, an increase of 24.4% compared to 2012 (US$534.50 million), while the amount held by Mexican borrowers increased 3.3%, going from US$335.48 million to US$346.55 million during the same period.

Changes in the monetary value of loans by state during the 12-month period ending December 31, 2013 are provided in Table 12. The only noteworthy change occurred in California, where loan investments in that state almost doubled from US$137.30 million to US$262.92 million during 2013, due to lending activity in the solar energy sector.

TABLE 11
Outstanding Loans by Environmental Sector
(US$ Millions)

	12/31/2013	12/31/2012	% Change
Wind energy	**$ 369.93**	$ 343.59	7.7%
Solar energy	**267.62**	159.96	67.3%
Water/wastewater	**158.84**	133.04	19.4%
Air quality	**118.62**	133.83	-11.4%
Storm drainage	**66.06**	69.15	-4.5%
Basic urban infrastructure*	**29.00**	26.71	8.6%
Other clean energy	**1.14**	1.73	-34.4%
Solid waste	**-**	1.97	-100.0%
Total	**$ 1,011.21**	$ 869.98	

* Basic urban infrastructure generally includes a mix of street paving, water and sewer lines, and storm drainage.

TABLE 12
Outstanding Loans by State*
(US$ Millions)

	12/31/2013	12/31/2012	% Change
Texas	**$ 313.20**	$ 325.97	-3.9%
California	**262.92**	137.30	91.5%
Tamaulipas	**165.64**	159.65	3.8%
Arizona	**88.54**	71.23	24.3%
Sonora	**81.08**	66.59	21.8%
Baja California	**58.96**	61.48	-4.1%
Nuevo Leon	**28.85**	38.45	-25.0%
Chihuahua	**9.04**	6.10	48.2%
Coahuila	**2.98**	3.21	-7.2%
Total	**$ 1,011.21**	$ 869.98	

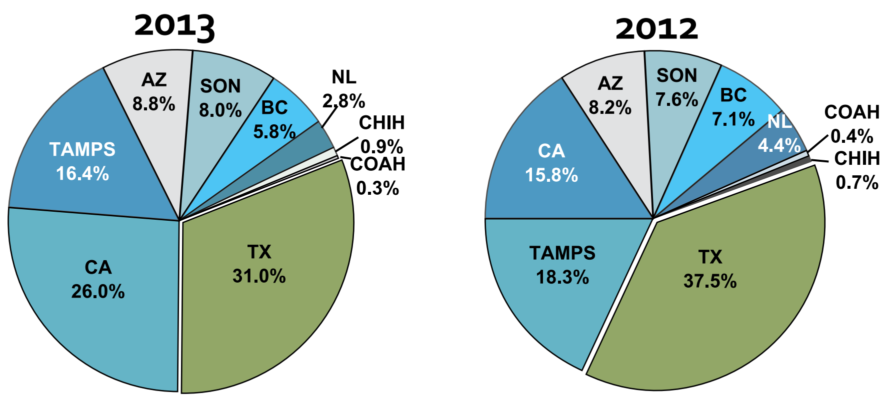
* Includes loans to both public and private borrowers.

In terms of portfolio distribution by state, more than 70% of loans outstanding continued to be concentrated in the same three states, although the distribution among those states shifted and was more evenly divided by the end of 2013, as illustrated in Figure 3. As of December 31, 2013, Texas accounted for 31.0% of the loan portfolio, down from 37.5% at the beginning of the period, followed by California with 26.0% (compared to 15.8% in 2012) and Tamaulipas with 16.4% (compared to 18.3% in 2012).

Non-performing Loans: The Bank monitors the credit quality of its borrowers on an ongoing basis and may suspend the disbursement of a loan in the event a weakness is identified that jeopardizes repayment in compliance with the contractual terms. 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.

FIGURE 3

Outstanding Loans by State



Loans are generally placed in nonaccrual status when principal or interest is delinquent for 180 days or more, or where reasonable doubt exists as to timely collection. Of the 61 loans in its portfolio at the close of 2013, two were classified as non-performing with an outstanding balance of US$6.98 million, representing less than one percent of the loan portfolio. In comparison, two of the 55 loans in its portfolio at the close of 2012 were classified as non-performing with an outstanding balance of US$13.82 million.

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, 2013, the Bank had a specific allowance for loan losses of US$3.44 million relating to one non-performing loan under the international program. In the case of the second non-performing loan, the Bank expects to recover the full amount due.

The Bank evaluates credit recovery actions on a case-by-case basis and negotiates with delinquent borrowers to recover amounts due. In certain cases where a borrower experiences financial difficulties, the Bank may seek to restructure the contractual terms of the loan.

Grant Operations

Under the international program, NADB uses a portion of its retained earnings to finance grant and technical assistance programs in support of its mandate. These funds may be designated by the Board as needed and are subject to availability. Having closed out the Solid Waste Environmental Program (SWEP) at the end of 2012, NADB had three grant programs in 2013: the Community Assistance Program (CAP), the Water Conservation Investment Fund (WCIF) and the Technical Assistance Program (TAP). The objectives and funding limits of each program are described in Box 3.

For fiscal years 2013 and 2012, US$0.45 million from undesignated retained earnings was allocated to the technical assistance program for training purposes. No new funding was allocated for grant financing during 2013; however, with the termination of the WCIF program, a total of US$1.06 million in uncommitted WCIF funds was rolled over to the CAP program, bringing total funding allocated to the CAP to US$11.47 million.

During 2013, NADB approved and contracted US$2.18 million in CAP grants to support the implementation of five infrastructure projects, while in 2012 one grant was approved and contracted for US$0.45 million through the SWEP program. New grant commitments for infrastructure projects averaged US$1.06 million annually during the past five years.

A small portion of CAP funding is used to cover the supervision costs of projects financed under the program. Approximately US$0.17 million was committed to construction supervision contracts in 2013. Therefore, as of December 31, 2013, NADB had a balance of US$9.12 million in uncommitted CAP funding available for future projects.

With respect to technical assistance, NADB approved US$0.57 million for five studies in 2013 and US$0.44 million for four studies in 2012. During the past five years, new grant approvals for technical assistance projects have averaged US$0.50 million annually.

Disbursements of NADB-funded grants for studies, training and project implementation for the years ended December 31, 2013 and 2012 came to US$1.14 million and US$2.44 million, respectively. Over the past five years, grant disbursements have averaged US$2.43 million annually. Lower-than-average disbursements in 2013 can be attributed to the closeout of the SWEP program at the end of 2012 and the fact that the CAP program was still in the startup phase in 2013. A breakdown of grant disbursements by program for the past two years is shown in Table 13.

The grant disbursements were funded with previously designated retained earnings. At the end of 2013, there was a balance of approximately US$6.16 million in committed grant funds pending disbursement: US$3.82 million for WCIF, US$2.35 million for CAP and US$0.36 million in TAP funds.

NADB also administers grant funds provided by EPA through the BEIF for 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 NADB's consolidated financial statements, but have no economic effect on its operations. During the years ended December 31, 2013 and 2012, NADB

Domestic Programs

As outlined in the Charter, 10% of NADB's subscribed capital was designated for community adjustment and investment programs in the two countries (the "domestic programs"). The funds for the Mexican domestic program were transferred in full to the Mexican government. In the case of the U.S. domestic program, NADB continues to hold and administer its funds. Consequently, its accounts are reported and included with those of NADB's international program. However, the U.S. domestic program's operations and allocated capital funding are completely independent of the Bank's international program, and any net income earned by the program and its profits, losses, expenses and disbursements do not affect the Bank's retained earnings or paid-in capital.

The U.S. domestic program called, Community Adjustment and Investment Program (USCAIP), was designed to assist communities and the private sector in creating new jobs and preserving existing jobs in areas adjusting to changes in their economies as a result of NAFTA. USCAIP operates under the direction of a Finance Committee that is comprised of representatives of the U.S. Departments of the Treasury, Agriculture (USDA), and Housing and Urban Development (HUD), and the U.S. Small Business Administration (SBA), along with other agencies selected by the Department of the Treasury, which serves as Finance Committee chair. NADB disburses USCAIP funds under the direction of the Finance Committee, which is responsible for endorsing all financing decisions under USCAIP.

In January 2009, the Finance Committee determined that the best way to use the remaining USCAIP capital and have the greatest possible impact on USCAIP eligible communities would be principally through a Targeted Grant Program. During 2013, US$0.83 million in grants was disbursed through this program, and six new grants totaling more than US$1.50 million were awarded and are expected to create 657 full-time, private sector jobs and preserve 966. During the same period, one loan was repaid in full. As of December 31, 2013, USCAIP had three loans with an outstanding balance of US$1.16 million.

Expenditures directly related to the operation of the Los Angeles and San Antonio offices of the U.S. domestic program are paid out of its capital funds. Expenditures for the fiscal years ended December 31, 2013 and 2012 totaled US$0.29 million and US$0.35 million, respectively.

For more information about the U.S. domestic program, see Note 8 in the Consolidated Financial Statements or visit the USCAIP website at www.nadbank-caip.org.

Funding Resources

NADB funds its lending activities and general operations with equity (paid-in capital and retained earnings) and the proceeds from borrowings. As of December 31, 2013, total equity under the international program was US$518.65 million as compared to US$521.85 million at the close of 2012.

Capitalization

The total authorized capital of NADB is US$3 billion with equal commitments from its two member countries, the United States and Mexico. Each government authorized the subscription of 150,000 shares of the Bank's capital stock with a par value of US$10,000 per share. Fifteen percent of NADB's authorized capital is in the form of paid-in capital and the remaining 85% is callable capital.

Paid-in capital: Paid-in capital consists of cash funds contributed to NADB by the U.S. and Mexico. As of May 2009, the Bank had received all paid-in capital contributions from the two governments, totaling US$450 million. As set forth in its Charter at inception, 10% of the paid-in capital and associated callable capital subscribed by each country went to finance the domestic programs. Therefore, of the US$450 million in paid-in capital, US$45 million was transferred to the domestic programs for community adjustment and investment, leaving US$405 million for NADB's international program.

The paid-in capital for the domestic programs was divided equally between the two countries with each receiving US$22.50 million for its respective program. The balance of paid-in capital and related earnings for the Mexican domestic program was subsequently transferred to the Mexican federal government as of June 1999. In the case of the U.S. domestic program, NADB continues to hold and administer the balance of its paid-in capital and related earnings. As of December 31, 2013, US$5.77 million in paid-in capital was allocated to USCAIP and held in the Bank's General Reserve.

Callable capital: Callable capital totaling US$2.55 billion—with US$255 million related to the domestic programs and the remaining US$2.295 billion to the international program—is composed of funds that must be provided to NADB by the two governments if required to meet its outstanding debt obligations or guaranties. Callable capital may not be used for loans or investments and constitutes, in effect, backing for the Bank's outstanding indebtedness and guaranties.

The subscription of US$1.275 billion of callable capital stock has been authorized by both governments through their respective legislatures and will be appropriated, if needed. Any capital call must be made uniformly to both member countries, but the obligations of the U.S. and Mexico to make payment of the callable portion of their capital subscriptions to the Bank are independent of each other. As a result, the failure of one member country to make payment on any such call would not excuse the other member from its obligation to make payment and, if necessary, the Bank may make successive calls on the non-defaulting member, up to its subscribed callable capital limit. Neither member country may be required to pay more than the unpaid balance of its capital subscription.

General Reserve

The Bank maintains a General Reserve funded in an amount equal to the retained earnings of NADB, plus transfers from paid-in capital for the U.S. domestic program. As of December 31, 2013 and 2012, the General Reserve balance was US$126.59 million and US$120.43 million, respectively, of which approximately US$121.70 million and US$114.48 million, respectively, related to the Bank's retained earnings under the international program. The remaining balances of US$4.89 million and US$5.95 million represented the allocated paid-in capital and retained earnings of the U.S. domestic program as of December 31, 2013 and 2012, respectively.

Retained earnings are classified as reserved for a specific purpose, designated to a specific program or undesignated. Under the international program NADB maintains four reserves, which are described and funded in the order of priority shown in Box 4.

BOX 4
Reserve Funds under the International Program

- **Debt Service Reserve:** 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:** Maintained in an amount equal to 12 months of the operating budget expenses at each fiscal year-end.
- **Special Reserve:** 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 US$30 million.
- **Capital Preservation Reserve:** Indexed to the U.S. annual inflation rate in order to maintain the value of the paid-in capital in real terms.

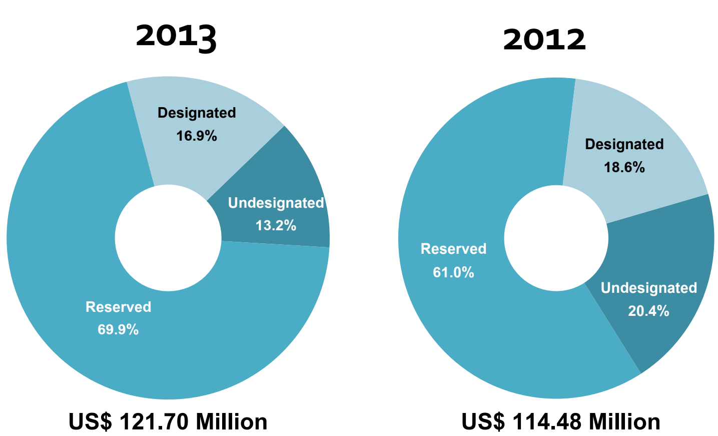
Annual allocations from undesignated retained earnings to the reserve funds are made as necessary, and if available, to maintain the levels mandated under the retained earnings policy. Allocations of undesignated retained earnings to programs may be made with Board approval only after full funding of the reserves. Table 14 provides a breakdown of the retained earnings allocated to reserves and programs at the end of fiscal years 2013 and 2012.

During 2013, retained earnings grew by 6.3%, to a total of US$121.70 million, while the amount allocated to reserves increased by 21.9%, mainly as a result of increased borrowing activity and capital preservation requirements, and the amount designated to programs decreased 3.4% due to grant disbursements. Consequently, at the close of 2013, 69.9% (US$85.11 million) of retained earnings was allocated to reserves and 16.9% (US$20.58 million) was designated to fund programs, leaving a balance of US$16.01 million in undesignated retained earnings.

TABLE 14
Reserved and Designated Retained Earnings under the International Program
(US$ Millions)

	12/31/2013	12/31/2012
Reserved retained earnings		
Debt Service Reserve	**$ 18.43**	$ 12.84
Operating Expenses Reserve	**9.38**	8.74
Special Reserve	**30.00**	27.30
Capital Preservation Reserve	**27.30**	20.91
Total reserves	**$ 85.11**	$ 69.79
Designated retained earnings		
Community Assistance Program (CAP)	**$ 11.47**	$ 10.42
Water Conservation Investment Fund (WCIF)	**3.82**	5.33
Technical Assistance Program (TAP)	**5.29**	5.54
Total designated	**$ 20.58**	$ 21.29

FIGURE 4
Retained Earnings under the International Program



The Special Reserve is used to offset any unexpected losses on outstanding loans or to pay expenses relating to the enforcement of the Bank's rights under outstanding loan and guaranty agreements. The U.S. domestic program may also allocate funding to this reserve for its loans. As of December 31, 2013 and 2012, special reserves allocated to the U.S. domestic program totaled US$34,667 and US$45,214, respectively.

Borrowings

NADB may raise 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. The Bank's annual borrowing plan is approved by the Board of Directors. Total principal outstanding debt may not exceed at any time the callable portion of its subscribed capital shares associated with the international program, plus the minimum liquidity level required under the liquidity policy. With US$2.295 billion in subscribed callable capital associated with the international program and a minimum liquidity level of US$185.5 million for 2014, the Bank's maximum debt limit at the close of 2013 was US$2.481 billion.

The Bank borrowed a total of US$316.39 million in 2013, compared to US$480 million in 2012. In October 2013, the Bank issued a five-year non-amortizing note with a face value of US$300.00 million at a fixed coupon rate that generated proceeds of US$298.21 million. In addition, under a fixed-rate loan agreement for up to US$50 million contracted with another development bank in November 2012, the Bank drew down US$16.39 million during 2013 to fund eligible wastewater projects in Mexico. For the years ended December 31, 2013 and 2012, the Bank had US$1.05 billion and US$730.00 million, respectively, in gross outstanding indebtedness. Most of the Bank's fixed-rate debt is hedged through interest rate swaps, effectively changing it to floating rates.

In April 2013, Fitch Ratings assigned NADB a credit rating of AA/F1+ with a stable outlook. In September 2013, Moody's Investors Service reaffirmed its Aaa/Prime-1 rating of NADB with a stable outlook. However, in December 2013, Moody's published a revised credit rating methodology for multilateral development banks and other supranational entities and placed NADB under review for a possible downgrade.

Results of Operations

Under the international program, the Bank's main source of revenue is derived from interest income on its loan portfolio and investment holdings. Expenses mainly consist of interest paid on borrowed funds, personnel and administrative costs, provisions for loan losses and swap expenses. The Bank has experienced positive income before program expenses (grant disbursements) in each year since its inception.

For the year ended December 31, 2013, the Bank had total revenue of US$39.58 million, total operating expenses of US$20.38 million, interest expense of US$10.84 million and income before program activities of US$8.37 million. Net income after program expenses (grant disbursements) was US$7.22 million. Table 15 provides a breakdown of the main operating income and expense categories for the years ended December 31, 2013 and 2012.

TABLE 15

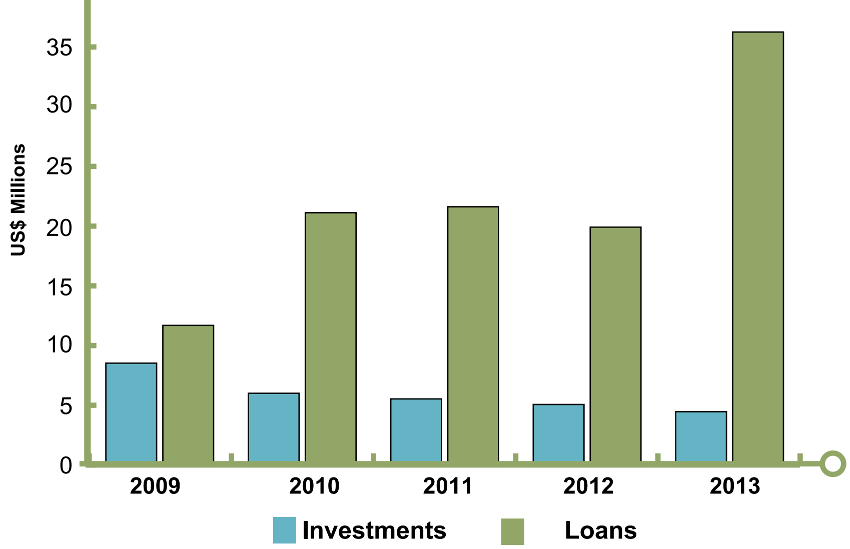
Operating Income & Expenses under the International Program
(US$ Millions)

	For the Year Ended 12/31/2013	For the Year Ended 12/31/2012
Loan interest income	**$ 35.15**	$ 19.34
Investment interest income	**4.39**	4.98
	39.54	24.32
Less: interest expense	**10.84**	5.36
Net interest income	**28.70**	18.96
Gain (loss) on sales of investments, net	**(0.01)**	2.80
Other income	**0.05**	0.59
Total net revenue	**28.74**	22.35
Less:		
Administrative expenses	**8.87**	8.42
Provisions for loan losses	**10.54**	-
Other expenses	**0.96**	2.98
Litigation expense	**-**	1.49
Income before program activities	**$ 8.37**	$ 9.46

Interest Income: For the year ended December 31, 2013, interest from loans totaled US$35.15 million, an increase of US$15.81 million or 81.7% over the previous year, reflecting the strong growth of the loan portfolio, which has doubled in the past two years.

Interest income on investments for the year ended December 31, 2013, remained fairly stable at US$4.39 million, compared to US$4.98 million at the end of 2012. The slight decrease can be attributed to lower average investment balances as securities were sold to fund new loans, as well as to prevailing market conditions.

FIGURE 5
Annual Interest Income



Net Gain (Loss) on Investments: The net loss on sales of available-for-sale investment securities for the year ended December 31, 2013, was less than US$0.01 million, as compared to a net gain of US$2.80 million for the year ended December 31, 2012. Available-for-sale investment securities totaled US$435.10 million as of December 31, 2013 and US$272.62 million as of December 31, 2012, representing an increase of US$162.47 million or 59.6%. This increase was mainly due to the proceeds of a debt issuance that were received in the last quarter of the year.

Other Income and Expenses: Other income and expenses consist of net foreign exchange gains (losses), net gains (losses) from swaps, loan fees, depreciation and other miscellaneous income and expenses. For the year ended December 31, 2013, other income totaled US$0.05 million as compared to US$0.59 million for the year ended December 31, 2012. The net decrease is primarily attributable to a US$0.33 million decrease in net foreign exchange gains and a US$0.21 million decrease in other miscellaneous income. For the years ended December 31, 2013 and 2012, other expenses totaled US$0.96 million and US$2.98 million, respectively. The decrease is mainly attributable to a US$2.08 net decrease in the fair value of swaps and a US$0.06 million increase in net foreign exchange loss.

Interest Expense: Interest expense consists of the interest on the US$1.05 billion and US$730 million in long-term debt as of December 31, 2013 and 2012, respectively, net of hedge effect. For the year ended December 31, 2013, interest expense totaled US$10.84 million as compared to US$5.36 million for the year ended December 31, 2012.

Provision for Loan Losses: During 2013, the allowance for loan losses was increased by US$10.54 million, mainly due to a provision for general loan losses totaling US$9.45 million, as the Bank implemented its new general allowance policy. The remaining US$1.09 million was provisioned for a specific impaired loan. No provision for loan loss was made in 2012.

Administrative Expenses: Administrative expenses, which consist of personnel, consultants, travel, general and administrative costs, grew 5.3%, from US$8.42 million in 2012 to US$8.87 million in 2013, primarily as a result of the growth of the Bank's operations. During the same period, the ratio of administrative expenses to outstanding loans declined from 0.97% in 2012 to 0.88% in 2013.

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.

Liquidity Policy

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. The minimum liquidity level is 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 2013 fiscal year was US$164.0 million and for the 2014 fiscal year it will be US$185.5 million.

The Bank's liquid asset holdings are in the form of cash, cash equivalents (mainly repurchase agreements) and investments in longer term marketable securities (fixed-income securities). All of the Bank's investments are classified as held-to-maturity or available-for-sale securities. Since securities designated as held-to-maturity are not considered liquid asset holdings for purposes of determining minimum liquidity, all of the investments held in the liquidity portfolio are designated as available-for-sale. As of December 31, 2013, 47.5% of the Bank's liquid asset portfolio was comprised of highly liquid assets (cash, cash equivalents and U.S. Treasuries). The remaining 52.5% was comprised of fairly liquid assets (all other types of liquid investment securities held by the Bank).

TABLE 16

Liquid Assets under the International Program

(US$ Millions)

Type of Security	For the Year Ended 12/31/2013	For the Year Ended 12/31/2012
Cash and Cash Equivalents	**$ 56.81**	$ 62.36
U.S. Treasury Securities	**176.81**	116.19
U.S. Agency Securities	**92.28**	44.74
Mortgage-backed Securities	**0.08**	0.34
United Mexican State (UMS) Securities	**18.37**	20.83
Taxable Municipal Securities	**5.08**	8.05
Other Permissible Securities*	**142.48**	82.47
Total	**$ 491.91**	$ 334.98

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

As of December 31, 2013 and 2012, liquid assets under the international program totaled US$491.91 million and US$334.98 million, respectively. The US$156.93 million increase in the liquid asset portfolio was primarily the result of the proceeds of borrowings, as well as loan principal and interest payments. At the close of 2013, the Bank's liquid assets represented 31.3% of total assets (US$1,573.08 million) and 47.0% of total gross debt (US$1,046.39 million), as compared to 25.7% of total assets (US$1,302.30 million) and 45.9% of total gross debt (US$730 million) at the end of 2012.

Investment Policy

The Bank's investment objectives are to ensure that its liquid assets are prudently invested to preserve capital and provide necessary liquidity.

The Bank only invests in high quality, highly-liquid securities which have readily identifiable prices. Permissible securities that otherwise meet the Bank's investment policy comprise a wide range of high-quality fixed-income instruments, including U.S. Treasury and governmental agency securities, Mexican government securities, bank deposits, repurchase agreements (pursuant to master purchase agreements and fully collateralized by U.S. Treasury securities), certificates of deposit, commercial paper and money market funds.

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 investment portfolio must contain a minimum of 25% U.S. government securities; all other securities are subject to caps as indicated in Box 5.

BOX 5

Investment Guidelines

Securities	Established Limits
U.S. Treasury securities	25% minimum
U.S. agency securities	45% maximum
Mortgage-backed securities	15% maximum
Mexican (UMS) securities	30% maximum
Taxable municipal securities	25% maximum
Other permissible securities	35% maximum

The majority of the securities in which the Bank invests 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. Repurchase agreements, certificates of deposit and commercial paper counterparties must have a short-term debt rating of A-1 (or its equivalent) or higher by a recognized securities rating agency.

Risk Management

As a part of its development financing services, the Bank is exposed to credit risk (loan portfolio or commercial credit/counterparty risk); market risk (interest rate and exchange rate); liquidity risk (funding and liquidation); and operational risk. The Bank manages its risks in accordance with its Charter and the policies approved by its Board of Directors. In general, NADB manages the risks inherent in its lending activities by ensuring that the projects it finances meet certain economic and feasibility criteria and by requiring some form of credit support. NADB's commercial risk is limited by its liquidity and investment policies. The Bank takes a conservative approach to market risk, which is neutralized or mitigated through the use of derivatives.

Credit Risk

The Bank is subject to certain credit risk related to the potential losses that could result from the default of borrowers (loan portfolio credit risk) or from the default of the Bank's investment, trading or swap counterparties (commercial credit or counterparty risk).

Loan Portfolio Credit Risk: As a result of its core business of providing infrastructure development loans, the Bank is exposed to the risk that it may not receive payment of principal and/or interest on one or more of its loans in accordance with the agreed-upon terms. Loan portfolio credit risk is determined by the credit quality of each borrower and the Bank's exposure to each borrower. The Bank mitigates this credit-default risk by performing thorough credit analyses and applying stringent due-diligence procedures to projects and borrowers, as well as using tailor-made loan structures with strong payment mechanisms and adhering to strict debt service coverage requirements. In addition, the Bank has established policies limiting its exposure per project and per obligor, and continually monitors the financial stability of each borrower throughout the term of the loan.

To further mitigate this credit default risk, all of the loans in the Bank's outstanding portfolio are secured by some form of credit support, including project revenue, borrower cash flows, senior liens on project equity and assets, step-in rights or, in the case of Mexican loans, federal tax revenue pledged to an irrevocable trust or pursuant to a mandate agreement. In addition, the Bank 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.

Commercial Credit and Counterparty Risks: Commercial credit risk is the exposure to losses that could occur as a result of the default of one of the Bank's investment, trading or swap counterparties. The main sources of the Bank's commercial credit 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 the relative credit standing of these financial institutions and limits the amount of credit exposure with any one institution. All of its swaps are with five counterparties, two of which are backed by the federal government of Mexico. The other three are commercial financial institutions, two of which are rated A2/A and the third is rated A2/A+ by two nationally-recognized rating agencies. NADB signs an International Swap and Derivatives Association (ISDA) agreement with the commercial banks with which it enters into swap transactions.

Liquidity Risk

Liquidity risk arises from a financial institution's inability to meet its contractual obligations in a timely manner without adversely affecting daily operations or the financial condition of the institution. NADB has established liquidity and investment policies to mitigate this risk. Under these policies, NADB maintains a portfolio of liquid investments to 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.

Market Risk

The Bank is exposed to market risks as a result of general market movements, mainly through changes in interest and exchange rates affecting earnings on its loan and investment portfolios and the cost of its external borrowings. These risks are mitigated through the Bank's asset and liability management program and its hedging activities.

Interest Rate Risk: There are three potential sources of interest rate risk for the Bank: (i) financial margin volatility from a mismatch in timing on the reset periods to maturity between assets and liabilities; (ii) changes in the market value of investments and redemption of investments to fund loans; and (iii) cost of external borrowings in loan pricing due to decrease in market interest during the term of borrowed funds.

To mitigate the volatility of the financial margin and minimize a repricing mismatch, the Bank uses interest rate swaps to hedge asset and liability positions. Most of the Bank's fixed-rate borrowings have been swapped to a floating interest rate. Fixed-rate loans made with the proceeds of the swapped debt are in turn swapped to a floating rate.

To minimize the risk related to investments, the Bank controls the average duration of its portfolio. To ensure the maintenance of adequate liquidity and to protect the Bank's portfolio from significant losses caused by interest rate movements, the average duration of the portfolio may not exceed four years. The Bank structures its investment portfolio so that its investment securities mature concurrent with anticipated cash flow requirements, with additional consideration for unanticipated cash demands.

Exchange Rate Risk: The Bank is exposed to exchange rate risk as a result of its dual-currency lending operations. To minimize exchange rate risk, NADB matches its lending operations to the local currency of the borrower. For U.S. borrowers, loans are available in U.S. dollars. For Mexican borrowers, loans are available in Mexican pesos, as well as in U.S. dollars if the project generates a U.S. dollar cash flow. For U.S. dollar loans to Mexican borrowers, the Bank must obtain assurance that the borrower will be able to generate the dollars to make payment when due before making the loan. For financing extended in pesos, a currency hedge must be established unless the source of funding for the loan is also in pesos.

COFIDAN, a non-regulated, multi-purpose financial institution established in Mexico to channel NADB loans to state and local public entities in that country, is wholly-owned by the Bank, and its accounts are consolidated with those of the Bank for financial reporting purposes. Since COFIDAN is located in Mexico, it operates primarily using Mexican pesos. Accordingly, the Bank is exposed to some exchange rate risk in the translation of COFIDAN's assets and liabilities into U.S. dollars using the exchange rate in effect at the end of the relevant financial reporting period (revenue and expenses are translated using average exchange rates for the period). The resulting cumulative translation adjustment is included in NADB's accumulated other comprehensive income. Because of the small asset size, such adjustments have not been material and are not expected to be in the future.

Operational Risk

Operational risk is the potential loss arising from external events or from internal activities due to inadequate or failed processes, a breakdown in systems or human error. Operational risk also includes fraud and failures in the execution of legal, fiduciary and agency 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. This system is strengthened by the Bank's highly qualified personnel who maintain the highest standards of integrity and professionalism in the performance of their duties.

In addition, NADB has an internal audit staff that reviews the Bank's operations and finances based on a continual risk assessment, with direction from Bank management. The internal audit staff is also vested with the responsibility of tracking loan and grant covenant compliance and reviewing monthly and quarterly statistical reports. The internal audit staff reports directly to Bank management and provides semiannual reports to the Board, which include an assessment of the effectiveness of NADB's internal control framework and any key internal audit findings, which are defined as anything that significantly impairs the achievement of the Bank's mission, the Bank's internal control system, the effective and efficient utilization of the Bank's assets or the safeguarding of the Bank's assets.

To further mitigate this risk and strengthen its internal controls, the Bank engaged a consultant in 2013 to perform a comprehensive operational risk assessment. In general, the assessment includes identifying and classifying areas subject to risk, assessing the likelihood of occurrence and their potential impact, reviewing the system of controls and procedures currently in place to monitor the Bank's processes, and providing recommendations for improvements. The final report will be delivered to the Bank in May 2014.

Basis of Reporting & Critical Accounting Policies

The Bank's consolidated financial statements are prepared in accordance with generally accepted accounting principles in the United States (GAAP), 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 to be 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 and reserves in the Bank's 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. 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 Bank's loan portfolio, and the allowance is maintained at a level considered adequate 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.

External Auditors

The accounts of the Bank are audited annually by independent external auditors of international reputation chosen by the Board on the basis of 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. Having completed a five-year term as the Bank's external auditors in 2011, Ernst & Young LLP (E&Y) won the bid in 2012 and was appointed by the Board as the Bank's external auditors for a second five-year term that will end in 2016. The Bank renewed its contract with E&Y to carry out the annual audit of its accounts for fiscal year 2013.

Consolidated Financial Statements and Supplemental Information

North American Development Bank
Years Ended December 31, 2013 and 2012
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, 2013 and 2012, 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, 2013 and 2012, 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 financial statements as a whole. The supplementary information is presented for purposes of additional analysis and is 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 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

March 31, 2014

Consolidated Balance Sheets

	December 31 2013	2012
Assets		
Cash and cash equivalents:		
Held at other financial institutions in demand deposit accounts	**$ 76,348**	$ 2,332,246
Held at other financial institutions in interest-bearing accounts	**39,527,978**	50,658,739
Repurchase agreements	**21,000,000**	13,900,000
	60,604,326	66,890,985
Held-to-maturity investment securities, at amortized cost	**53,619,703**	53,593,008
Available-for-sale investment securities, at fair value	**435,095,011**	272,623,600
Loans outstanding	**1,012,367,164**	871,487,688
Allowance for loan losses	**(12,917,307)**	(2,373,188)
Unamortized loan fees	**(3,411,490)**	(1,846,488)
Foreign currency exchange rate adjustment	**(16,054,882)**	(15,521,405)
Hedged items, at fair value	**(17,343,992)**	9,451,273
Net loans outstanding	**962,639,493**	861,197,880
Interest receivable	**10,331,837**	8,515,615
Grant and other receivable	**419,481**	1,138,950
Furniture, equipment and leasehold improvements, net	**192,950**	134,968
Other assets	**55,079,144**	44,171,828
Total assets	**$ 1,577,981,945**	$ 1,308,266,834
Liabilities and equity		
Liabilities:		
Accounts payable	**$ 993,536**	$ 1,069,242
Accrued liabilities	**322,356**	237,609
Accrued interest payable	**8,343,188**	6,664,697
Undisbursed grant funds	**1,005**	1,005
Other liabilities	**37,650,115**	19,115,034
Long-term debt, net of discount	**1,041,314,034**	724,975,593
Hedged items, at fair value	**(34,189,989)**	28,404,469
Long-term debt, net	**1,007,124,045**	753,380,062
Total liabilities	**1,054,434,245**	780,467,649
Equity:		
Paid-in capital	**405,000,000**	405,000,000
General Reserve:		
Allocated paid-in capital	**5,773,589**	6,602,838
Retained earnings:		
Designated	**19,663,688**	20,597,256
Reserved	**85,140,670**	69,834,231
Undesignated	**16,013,735**	23,393,315
Accumulated other comprehensive income (loss)	**(8,050,355)**	2,365,011
Minority interest	**6,373**	6,534
Total equity	**523,547,700**	527,799,185
Total liabilities and equity	**$ 1,577,981,945**	$ 1,308,266,834

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

Consolidated Statements of Income

	Year Ended December 31	
	2013	**2012**
Income:		
Interest:		
Investment income	**$ 4,395,364**	$ 4,980,289
Loan income	**35,205,952**	19,445,850
Gain (loss) on sales of available-for-sale investment securities, net	**(8,011)**	2,801,888
Fee income	**46,261**	39,478
Other	**100**	550,233
Total revenues	**39,639,666**	27,817,738
Operating expenses:		
Personnel	**5,193,127**	5,332,143
Consultants	**2,346,345**	1,845,059
General and administrative	**1,049,866**	937,290
Operational travel	**281,591**	311,044
Depreciation and amortization	**35,480**	30,812
Provision for loan losses	**10,544,119**	–
Other	**926,792**	2,951,135
U.S. Domestic Program	**286,147**	348,188
Total operating expenses	**20,663,467**	11,755,671
Interest expense	**10,838,179**	5,362,742
Litigation expense	**–**	1,484,454
Income before program activities	**8,138,020**	9,214,871
Program activities:		
U.S. Environmental Protection Agency (EPA) grant income	**1,207,801**	1,589,277
EPA grant administration expense	**(1,207,801)**	(1,589,277)
Technical Assistance Program expense	**(689,865)**	(688,313)
Solid Waste Environmental Program expense	**–**	(1,050,691)
Water Conservation Investment Fund expense	**(455,025)**	(698,422)
Net program expenses	**(1,144,890)**	(2,437,426)
Income before minority interest	**6,993,130**	6,777,445
Net income (loss) attributable to minority interest	**(161)**	196
Net income attributable to NADB	**$ 6,993,291**	$ 6,777,249

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

Consolidated Statements of Comprehensive Income

	Year Ended December 31	
	2013	**2012**
Net income	**$ 6,993,291**	$ 6,777,249
Other comprehensive income (loss):		
Available-for-sale investment securities:		
Change in unrealized gains (losses) during the period, net	**(1,164,800)**	804,882
Reclassification adjustment for net (gains) losses included in net income	**8,011**	(2,801,888)
Total unrealized loss on available-for-sale investment securities	**(1,156,789)**	(1,997,006)
Foreign currency translation adjustment	**(41,184)**	(29,872)
Unrealized gains (losses) on hedging activities:		
Foreign currency translation adjustment, net	**(5,532)**	18,117,110
Fair value of cross-currency interest rate swaps, net	**(9,211,861)**	(34,459,499)
Total unrealized loss on hedging activities	**(9,217,393)**	(16,342,389)
Total other comprehensive loss	**(10,415,366)**	(18,369,267)
Total comprehensive loss	**$ (3,422,075)**	$ (11,592,018)

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)	Minority Interest	Total Equity
Beginning balance, January 1, 2012	$ 405,000,000	$ 8,111,717	$ 107,047,553	$ 20,734,278	$ 6,338	$ 540,899,886
Transfer to Targeted Grant Program of the U.S. Domestic Program	–	(1,508,879)	–	–	–	(1,508,879)
Net income	–	–	6,777,249	–	–	6,777,249
Other comprehensive income	–	–	–	(18,369,267)	–	(18,369,267)
Minority interest	–	–	–	–	196	196
Ending balance, December 31, 2012	405,000,000	6,602,838	113,824,802	2,365,011	6,534	527,799,185
Transfer to Targeted Grant Program of the U.S. Domestic Program	**–**	**(829,249)**	**–**	**–**	**–**	**(829,249)**
Net income	**–**	**–**	**6,993,291**	**–**	**–**	**6,993,291**
Other comprehensive loss	**–**	**–**	**–**	**(10,415,366)**	**–**	**(10,415,366)**
Minority interest	**–**	**–**	**–**	**–**	**(161)**	**(161)**
Ending balance, December 31, 2013	**$ 405,000,000**	**$ 5,773,589**	**$ 120,818,093**	**$ (8,050,355)**	**$ 6,373**	**$ 523,547,700**

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

Consolidated Statements of Cash Flows

	Year Ended December 31	
	2013	2012
Operating activities		
Net income	**$ 6,993,291**	$ 6,777,249
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	**35,480**	30,812
Amortization of net premium on investments	**1,980,067**	1,589,964
Change in fair value of swaps	**(26,463,294)**	5,953,352
Minority interest	**(161)**	196
Gain (loss) on sales of available-for-sale investment securities, net	**8,011**	(2,801,888)
Provision for loan losses	**10,544,119**	–
Change in other assets and liabilities:		
(Increase) decrease in interest receivable	**(1,816,222)**	139,320
(Increase) decrease in receivable and other assets	**(7,605,846)**	1,659,152
Decrease in accounts payable	**(75,706)**	(2,651,756)
Increase (decrease) in accrued liabilities	**84,747**	(21,104)
Increase in accrued interest payable	**1,678,491**	1,301,061
Net cash provided by (used in) operating activities	**(14,637,023)**	11,976,358
Lending, investing, and development activities		
Capital expenditures	**(93,406)**	(49,071)
Loan principal repayments	**74,084,868**	54,487,202
Loan disbursements	**(214,964,344)**	(501,500,107)
Purchase of held-to-maturity investments	**(1,150,000)**	(3,773,000)
Purchase of available-for-sale investments	**(558,724,883)**	(420,233,920)
Proceeds from maturities of held-to-maturity investments	**1,145,000**	3,120,000
Proceeds from sales and maturities of available-for-sale investments	**393,086,910**	407,676,321
Net cash used in lending, investing, and development activities	**(306,615,855)**	(460,272,575)
Financing activities		
Proceeds from other borrowings	**16,386,468**	–
Proceeds from note issuance	**299,409,000**	475,410,400
Grant funds from the Environmental Protection Agency (EPA)	**18,976,292**	12,645,938
Grant disbursements – EPA	**(18,976,292)**	(12,645,937)
Grant activity – U.S. Domestic Program	**(829,249)**	(1,508,879)
Net cash provided by financing activities	**314,966,219**	473,901,522
Net increase (decrease) in cash and cash equivalents	**(6,286,659)**	25,605,305
Cash and cash equivalents at January 1, 2013 and 2012	**66,890,985**	41,285,680
Cash and cash equivalents at December 31, 2013 and 2012	**$ 60,604,326**	$ 66,890,985
Supplemental cash information		
Cash paid during the year for interest	**$ 23,055,486**	$ 10,937,500
Significant noncash transactions		
Foreign currency translation adjustment	**$ (5,533)**	$ 18,117,110
Change in fair value of cross-currency interest rate swaps, net	**$ (9,211,860)**	$ (34,459,499)
Change in fair value of available-for-sale investments, net	**$ (1,156,789)**	$ (1,997,006)

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

1. Organization and Purpose

The North American Development Bank (NADB or the Bank) was established 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 environmental infrastructure projects in the U.S.-Mexico border region (the International Program) and community adjustment and investment projects throughout the U.S. and Mexico in support of the purposes of the North American Free Trade Agreement (NAFTA) (the Domestic Programs). On March 16, 1994, the President of the United States issued an Executive Order designating the Bank an international organization under the International Organization Immunities Act.

The Bank began its operations on November 10, 1994, with initial capital subscriptions by the United States and Mexico. 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, as amended on August 6, 2004. The geographic jurisdiction of the International Program is within 100 kilometers north of the U.S.-Mexico border and within 300 kilometers south of the border.

Under its International Program, the Bank provides loan and grant financing and technical assistance for environmental infrastructure projects certified by the Border Environment Cooperation Commission (BECC), as appropriate, and administers grant funding provided by other entities. Under the Domestic Programs, the Bank contributed funds from its equity to establish the 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, 2013, COFIDAN is 99.90% owned by the Bank and 0.10% owned by the Mexican government. The accounts of COFIDAN are consolidated with the Bank, and all material intercompany accounts and transactions are eliminated in consolidation. The minority interest reflected in the consolidated balance sheets and consolidated statements of income represents the ownership of the Mexican government through the Ministry of Finance and Public Credit (SHCP).

The Bank is located in San Antonio, Texas. An additional office has been established in Los Angeles, California, to assist the United States in administering the U.S. Domestic Program.

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 accounting principles generally accepted in the United States of America (GAAP). The financial statements 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 investments, allowance for loan losses, the fair value of derivative instruments and other real estate owned included in other assets, the fair value of derivative instruments included in other liabilities, and long-term debt. Actual results could differ from those estimates.

2. Summary of Significant Accounting Policies (continued)

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 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, 2013 and 2012.

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.

2. Summary of Significant Accounting Policies (continued)

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 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 further 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 allowance for unallocated 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 investment in the loan asset. If collection of the recorded investment 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 monetary concessions to the borrower through modifications of the contractual terms of the loan, the loan is classified as a restructured troubled loan. 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. The determination of the allowance for loan losses is based on management’s current judgment about the credit quality of the loan portfolio. A specific allowance is established for impaired loans that exhibit a distinct possibility 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, allowances on loans to private-sector borrowers were established based on their statistical cumulative default rate, less their estimated recovery.

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

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

2. Summary of Significant Accounting Policies (continued)

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.

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

Program income represents reimbursed administrative expenses associated with the U.S. Environmental Protection Agency (EPA) grant activities. Such amounts are earned and recognized as program income in the accompanying consolidated statements of income as the associated expenses are incurred.

Program expenses include grant disbursements made by the Bank and administrative costs associated with EPA grant activities. 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 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, 2013, 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 three other financial institutions. The foreign currency translation adjustment on loans denominated in Mexican pesos as of December 31, 2013 and 2012 was $(16,054,882) and $(15,521,405), 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 in other income or expense. The fair value of these hedges was reported in the accompanying consolidated balance sheets at December 31, 2013 as other assets of $30,093,188 and other liabilities of $6,251,708 and at December 31, 2012 as other assets of $22,321,693 and other liabilities of $15,701,591.

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, 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 certain counterparties are subject to a master netting arrangement. Fair-value amounts recognized for derivatives and for the right or obligation to reclaim or return cash collateral are offset 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, and the fair value of hedged items where independent pricing information is not available for a significant portion of the underlying assets. For these financial instruments, 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 Bank's financial instruments 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)

Other Income and Other Expenses

Other income and other expenses consist primarily of net foreign exchange gains (losses) and net gains (losses) from swaps.

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, 2013 and 2012:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2013				
Held-to-maturity:				
U.S. agency securities	**$ 3,778,000**	**$ 2,033**	**$ (2,430)**	**$ 3,777,603**
Mexican government securities (UMS)	**49,841,703**	**5,558,297**	**–**	**55,400,000**
Total held-to-maturity investment securities	**53,619,703**	**5,560,330**	**(2,430)**	**59,177,603**
Available-for-sale:				
U.S. government securities	**176,847,338**	**68,756**	**(110,413)**	**176,805,681**
U.S. agency securities	**92,580,053**	**3,259**	**(301,900)**	**92,281,412**
Corporate debt securities	**105,040,656**	**54,732**	**(494,020)**	**104,601,368**
Other fixed-income securities	**42,907,758**	**92,294**	**(44,848)**	**42,955,204**
Mexican government securities (UMS)	**18,415,253**	**–**	**(42,753)**	**18,372,500**
Mortgage-backed securities	**75,212**	**3,634**	**–**	**78,846**
Total available-for-sale investment securities	**435,866,270**	**222,675**	**(993,934)**	**435,095,011**
Total investment securities	**$ 489,485,973**	**$ 5,783,005**	**$ (996,364)**	**$ 494,272,614**
December 31, 2012				
Held-to-maturity:				
U.S. agency securities	$ 3,773,000	$ 9,327	$ (321)	$ 3,782,006
Mexican government securities (UMS)	49,820,008	9,929,992	–	59,750,000
Total held-to-maturity investment securities	53,593,008	9,939,319	(321)	63,532,006
Available-for-sale:				
U.S. government securities	116,018,926	200,711	(25,833)	116,193,804
U.S. agency securities	44,684,047	85,573	(25,764)	44,743,856
Corporate debt securities	63,691,109	80,437	(96,655)	63,674,891
Other fixed-income securities	26,657,532	190,251	(7,148)	26,840,635
Mexican government securities (UMS)	20,854,913	23,717	(48,630)	20,830,000
Mortgage-backed securities	331,543	8,871	–	340,414
Total available-for-sale investment securities	272,238,070	589,560	(204,030)	272,623,600
Total investment securities	$ 325,831,078	$ 10,528,879	$ (204,351)	$ 336,155,606

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, 2013 and 2012:

	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2013						
Held-to-maturity:						
U.S. agency securities	**$ 1,657,570**	**$ 2,430**	**$ –**	**$ –**	**$ 1,657,570**	**$ 2,430**
Mexican government securities (UMS)	**–**	**–**	**–**	**–**	**–**	**–**
Total held-to-maturity investment securities	**1,657,570**	**2,430**	**–**	**–**	**1,657,570**	**2,430**
Available-for-sale:						
U.S. government securities	**101,158,872**	**110,413**	**–**	**–**	**101,158,872**	**110,413**
U.S. agency securities	**76,008,856**	**301,900**	**–**	**–**	**76,008,856**	**301,900**
Corporate debt securities	**80,252,396**	**494,020**	**–**	**–**	**80,252,396**	**494,020**
Other fixed-income securities	**24,365,068**	**44,848**	**–**	**–**	**24,365,068**	**44,848**
Mexican government securities (UMS)	**18,372,500**	**42,753**	**–**	**–**	**18,372,500**	**42,753**
Mortgaged-backed securities	**–**	**–**	**–**	**–**	**–**	**–**
Total available-for-sale investment securities	**300,157,692**	**993,934**	**–**	**–**	**300,157,692**	**993,934**
Total temporarily impaired securities	**$ 301,815,262**	**$ 996,364**	**$ –**	**$ –**	**$ 301,815,262**	**$ 996,364**
December 31, 2012						
Held-to-maturity:						
U.S. agency securities	$ 509,679	$ 321	$ –	$ –	$ 509,679	$ 321
Mexican government securities (UMS)	–	–	–	–	–	–
Total held-to-maturity investment securities	509,679	321	–	–	509,679	321
Available-for-sale:						
U.S. government securities	10,030,095	25,833	–	–	10,030,095	25,833
U.S. agency securities	12,368,404	25,764	–	–	12,368,404	25,764
Corporate debt securities	36,563,204	96,655	–	–	36,563,204	96,655
Other fixed-income securities	14,012,530	7,148	–	–	14,012,530	7,148
Mexican government securities (UMS)	6,960,000	48,630	–	–	6,960,000	48,630
Mortgaged-backed securities	–	–	–	–	–	–
Total available-for-sale investment securities	79,934,233	204,030	–	–	79,934,233	204,030
Total temporarily impaired securities	$ 80,443,912	$ 204,351	$ –	$ –	$ 80,443,912	$ 204,351

3. Investments (continued)

None of the unrealized losses identified above are considered to be other-than-temporary since, as of December 31, 2013, the Bank did not have the intent to sell any of the securities in the table above 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.

Contractual maturities of investments as of December 31, 2013 and 2012 are summarized in the following tables:

	Held-to-Maturity Securities		Available-for-Sale Securities	
	Fair Value	**Amortized Cost**	**Fair Value**	**Amortized Cost**
December 31, 2013				
Less than 1 year	**$ –**	**$ –**	**$ 261,396,676**	**$ 261,395,009**
1–5 years	**3,777,603**	**3,778,000**	**173,619,489**	**174,396,049**
5–10 years	**55,400,000**	**49,841,703**	**–**	**–**
More than 10 years	**–**	**–**	**–**	**–**
Mortgage-backed securities	**–**	**–**	**78,846**	**75,212**
	$ 59,177,603	**$ 53,619,703**	**$ 435,095,011**	**$ 435,866,270**
December 31, 2012				
Less than 1 year	$ –	$ –	$ 104,105,061	$ 104,073,861
1–5 years	3,782,006	3,773,000	161,265,576	160,903,375
5–10 years	59,750,000	49,820,008	6,912,549	6,929,291
More than 10 years	–	–	–	–
Mortgage-backed securities	–	–	340,414	331,543
	$ 63,532,006	$ 53,593,008	$ 272,623,600	$ 272,238,070

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, 2013 and 2012:

	Year Ended December 31	
	2013	**2012**
Held-to-maturity investment securities:		
Proceeds from maturities	**$ 1,145,000**	$ 3,120,000
Available-for-sale investment securities:		
Proceeds from sales and maturities	**393,086,910**	407,676,321
Gross realized gains	**261,809**	2,854,653
Gross realized losses	**269,820**	52,765

3. Investments (continued)

The following table sets forth the unrealized gains (loss) on securities available-for-sale and the reclassification adjustments required for the years ended December 31, 2013 and 2012:

	December 31	
	2013	**2012**
Unrealized gains on investment securities available-for-sale, beginning of year	**$ 385,530**	$ 2,382,536
Unrealized gains (losses) on investment securities available-for-sale, arising during the year	**(1,164,800)**	804,882
Reclassification adjustments for (gains) losses on investment securities available-for-sale included in net income	**8,011**	(2,801,888)
Unrealized gains (losses) on investment securities available-for-sale, end of year	**$ (771,259)**	$ 385,530

4. Loans

The following schedule summarizes loans outstanding as of December 31, 2013 and 2012:

	International Program	U.S. Domestic Program	Total
December 31, 2013			
Loan balance	**$ 1,011,211,596**	**$ 1,155,568**	**$ 1,012,367,164**
Allowance for loan losses:			
General	**(9,453,064)**	**(23,188)**	**(9,476,252)**
Specific	**(3,441,055)**	**–**	**(3,441,055)**
Unamortized loan fees	**(3,411,490)**	**–**	**(3,411,490)**
Foreign currency exchange rate adjustment	**(16,054,882)**	**–**	**(16,054,882)**
Fair value of hedged items	**(17,343,992)**	**–**	**(17,343,992)**
Net loans outstanding	**$ 961,507,113**	**$ 1,132,380**	**$ 962,639,493**
December 31, 2012			
Loan balance	$ 869,980,535	$ 1,507,153	$ 871,487,688
Allowance for loan losses:			
General	–	(23,188)	(23,188)
Specific	(2,350,000)	–	(2,350,000)
Unamortized loan fees	(1,846,488)	–	(1,846,488)
Foreign currency exchange rate adjustment	(15,521,405)	–	(15,521,405)
Fair value of hedged items	9,451,273	–	9,451,273
Net loans outstanding	$ 859,713,915	$ 1,483,965	$ 861,197,880

At December 31, 2013 and 2012, the International Program had outstanding loan commitments on signed loan agreements totaling $238,780,007 and $119,818,567, respectively. At December 31, 2013 and 2012, the U.S. Domestic Program did not have any outstanding loan commitments on signed loan agreements. The Board has also approved an additional $123,743,890 in loans for the International Program, for which loan agreements are in development.

4. Loans (continued)

The Bank under certain circumstances offered below-market-rate loans. As of December 31, 2013 and 2012, the Bank had below-market-rate loans outstanding for the International Program of $50,353,220 and $53,764,754, respectively, and for the U.S. Domestic Program of $0 and $297,362, respectively.

The following table presents the Bank's loan portfolio by sector as of December 31, 2013 and 2012:

	December 31 2013	December 31 2012
International Program:		
Air Quality	**$ 118,618,859**	$ 133,825,387
Basic Urban Infrastructure	**29,004,705**	26,712,282
Clean Energy:		
Solar	**267,622,888**	159,957,113
Wind	**369,929,600**	343,589,423
Other	**1,136,359**	1,731,113
Storm Drainage	**66,057,730**	69,153,364
Solid Waste	**–**	1,969,274
Water and Wastewater	**158,841,455**	133,042,579
Total International Program	**1,011,211,596**	869,980,535
U.S. Domestic Program	**1,155,568**	1,507,153
	$ 1,012,367,164	$ 871,487,688

The following table presents the loan portfolio by risk category as of December 31, 2013 and 2012. These risk categories are defined in Note 2, along with additional information on how the Bank evaluates credit quality.

	December 31 2013	December 31 2012
International Program:		
Pass	**$ 1,004,236,219**	$ 859,851,786
Special Mention	**3,693,738**	–
Substandard	**–**	–
Doubtful	**3,281,639**	10,128,749
Total International Program	**1,011,211,596**	869,980,535
U.S. Domestic Program:		
Pass	**763,578**	1,107,153
Special Mention	**391,990**	–
Substandard	**–**	400,000
Doubtful	**–**	–
Total U.S. Domestic Program	**1,155,568**	1,507,153
	$ 1,012,367,164	$ 871,487,688

4. Loans (continued)

The International Program had two nonaccrual loans with an outstanding balance of $6,975,377 and $13,822,487 as of December 31, 2013 and 2012, respectively. The average impaired loan balance for the years ended December 31, 2013 and 2012 totaled $13,251,894 and $14,908,599, respectively. No interest income was recognized on the impaired loans for the years ended December 31, 2013 and 2012. In March 2012, the Bank foreclosed on the collateral of a loan under the International Program with an outstanding balance, net of allowance for loan loss, of $800,000. In October 2012 and February 2013, a portion of this collateral was sold for a total of $146,693 in cash. In December 2013, the Bank foreclosed on the collateral of a loan under the International Program with an outstanding balance, net of allowance for loan loss, of $7,179,731, and received that amount as partial payment. The collateral from the foreclosed loans is reported as other assets of $7,833,038 and $680,002 as of December 31, 2013 and 2012, respectively.

The outstanding balance of loans past due 90 days or more that was still accruing interest was $77,619 and $98,216 as of December 31, 2013 and 2012, respectively.

An age analysis of past-due loans, including both accruing and non-accruing loans, as of December 31, 2013 and 2012, is shown in the following table.

4. Loans (continued)

Public-private are loans to private-sector borrowers backed by public-sector federal tax revenues.

The following schedule summarizes the allowance for the loan losses for the years ended December 31, 2013 and 2012:

	Allowance for Loan Losses				
	Beginning Balance	Specific	General	Loan (Chargeoffs) Recoveries	Ending Balance
December 31, 2013					
International Program:					
Private:					
Construction	**$ –**	**$ –**	**$ 4,950,438**	**$ –**	**$ 4,950,438**
Operation	**2,350,000**	**1,091,055**	**4,502,626**	**–**	**7,943,681**
Public	**–**	**–**	**–**	**–**	**–**
Public-private	**–**	**–**	**–**	**–**	**–**
Total International Program	**2,350,000**	**1,091,055**	**9,453,064**	**–**	**12,894,119**
U.S. Domestic Program	**23,188**	**–**	**–**	**–**	**23,188**
	$ 2,373,188	**$ 1,091,055**	**$ 9,453,064**	**$ –**	**$ 12,917,307**
December 31, 2012					
International Program:					
Private:					
Construction	$ –	$ –	$ –	$ –	$ –
Operation	8,066,672	–	–	(5,716,672)	2,350,000
Public	–	–	–	–	–
Public-private	–	–	–	–	–
Total International Program	8,066,672	–	–	(5,716,672)	2,350,000
U.S. Domestic Program	23,188	–	–	–	23,188
	$ 8,089,860	$ –	$ –	$ (5,716,672)	$ 2,373,188

The provisions for loan losses for the year ended December 31, 2013, and the loan charge-off for the year ended December 31, 2012, pertain to the International Program.

Additional funds are included within the Special Reserve as described in Note 2.

5. Other Assets and Other Liabilities

The following table presents the gross and net balances of other assets and other liabilities, including the result of master netting arrangements for derivatives with certain swap counterparties, at December 31, 2013 and 2012:

	Gross Amount	Master Netting Arrangements	Net Amount
December 31, 2013			
Other assets			
Cross-currency interest rate swaps	**$ 20,413,506**	**$ (354,448)**	**$ 20,059,058**
Interest rate swaps	**26,962,548**	**–**	**26,962,548**
Collateral from swap counterparty	**(4,800,000)**	**–**	**(4,800,000)**
Unamortized debt issuance costs	**5,024,500**	**–**	**5,024,500**
Other real estate owned	**7,833,038**	**–**	**7,833,038**
Total other assets	**$ 55,433,592**	**$ (354,448)**	**$ 55,079,144**
Other liabilities			
Cross-currency interest rate swaps	**$ 7,571,012**	**$ (964,396)**	**$ 6,606,616**
Interest rate swaps	**51,236,082**	**(472,583)**	**50,763,499**
Collateral to swap counterparty	**(19,720,000)**	**–**	**(19,720,000)**
Total other liabilities	**$ 39,087,094**	**$ (1,436,979)**	**$ 37,650,115**
December 31, 2012			
Other assets			
Cross-currency interest rate swaps	$ 22,692,834	$ (371,141)	$ 22,321,693
Interest rate swaps	33,573,698	(1,755,786)	31,817,912
Collateral from swap counterparty	(14,500,000)	–	(14,500,000)
Unamortized debt issuance costs	3,852,221	–	3,852,221
Other real estate owned	680,002	–	680,002
Total other assets	$ 46,298,755	$ (2,126,927)	$ 44,171,828
Other liabilities			
Cross-currency interest rate swaps	$ 7,775,100	$ (77,317)	$ 7,697,783
Interest rate swaps	11,913,941	(496,690)	11,417,251
Total other liabilities	$ 19,689,041	$ (574,007)	$ 19,115,034

6. Long-term Debt

The following table summarizes the long-term debt as of December 31, 2013 and 2012:

			December 31, 2013			
Issue Date	Maturity Date	Fixed Rate	Principal Amount	Unamortized Discount	Fair Value of Hedged Items	Long-term Debt, Net
Notes Payable						
Feb. 11, 2010	Feb. 11, 2020	4.375%	**$ 250,000,000**	**$ (398,750)**	**$ 16,928,418**	**$ 266,529,668**
Oct. 26, 2012	Oct. 26, 2022	2.400	**250,000,000**	**(758,472)**	**(21,754,994)**	**227,486,534**
Dec. 17, 2012	Oct. 26, 2022	2.400	**180,000,000**	**(3,337,508)**	**(18,061,814)**	**158,600,678**
Dec. 17, 2012	Dec. 17, 2030	3.300	**50,000,000**	**–**	**(8,975,878)**	**41,024,122**
Oct. 10, 2013	Oct. 10, 2018	2.300	**300,000,000**	**(577,703)**	**(2,325,721)**	**297,096,576**
Total Notes Payable			**1,030,000,000**	**(5,072,433)**	**(34,189,989)**	**990,737,578**
Other Borrowings						
Mar. 7, 2013	Dec. 30, 2015	1.900%	**2,631,000**	**–**	**–**	**2,631,000**
Mar. 7, 2013	Jun. 30, 2016	1.900	**1,653,972**	**–**	**–**	**1,653,972**
Aug. 15, 2013	Jun. 30, 2016	1.900	**977,028**	**–**	**–**	**977,028**
Aug. 15, 2013	Dec. 30, 2016	1.900	**2,631,000**	**–**	**–**	**2,631,000**
Aug. 15, 2013	Jun. 30, 2017	1.900	**2,631,000**	**–**	**–**	**2,631,000**
Aug. 15, 2013	Dec. 30, 2017	1.900	**2,631,000**	**–**	**–**	**2,631,000**
Aug. 15, 2013	Jun. 30, 2018	1.900	**2,631,000**	**–**	**–**	**2,631,000**
Aug. 15, 2013	Dec. 30, 2018	1.900	**600,467**	**–**	**–**	**600,467**
Total Other Borrowings			**16,386,467**	**–**	**–**	**16,386,467**
			$ 1,046,386,467	**$ (5,072,433)**	**$ (34,189,989)**	**$ 1,007,124,045**

			December 31, 2012			
Issue Date	Maturity Date	Fixed Rate	Principal Amount	Unamortized Discount	Fair Value of Hedged Items	Long-term Debt, Net
Feb. 11, 2010	Feb. 11, 2020	4.375%	$ 250,000,000	$ (464,000)	$ 31,817,912	$ 281,353,912
Oct. 26, 2012	Oct. 26, 2022	2.400	250,000,000	(844,472)	496,690	249,652,218
Dec. 17, 2012	Oct. 26, 2022	2.400	180,000,000	(3,715,935)	(2,388,403)	173,895,662
Dec. 17, 2012	Dec. 17, 2030	3.300	50,000,000	–	(1,521,730)	48,478,270
			$ 730,000,000	$ (5,024,407)	$ 28,404,469	$ 753,380,062

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. Unamortized debt issuance costs related to these notes, which are included in other assets, totaled $5,024,500 and $3,852,221 at December 31, 2013 and 2012.

6. Long-term Debt (continued)

The fair value of the hedges relating to interest rate swaps on a portion of the notes payable was reported at December 31, 2013 as other assets of $16,928,418 and other liabilities of $51,118,407, and at December 31, 2012 as other assets of $31,817,912 and other liabilities of $3,413,443. See Notes 11 and 12 for additional information on the fair value of financial instruments and derivatives, respectively.

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 will amortize semi-annually, with the first principal payment payable on December 30, 2015 and final principal payment payable on December 30, 2024. As of December 31, 2013, the Bank has borrowed $16,386,467. An annual commitment fee of 0.25% was assessed on the undisbursed loan commitment beginning in May 2013. As of December 31, 2013, these fees totaled $46,032.

The following table summarizes the maturities of the long-term debt as of December 31, 2013 and 2012:

	December 31 2013	December 31 2012
Less than 1 year	**$ –**	$ –
1–2 years	**2,631,000**	–
2–3 years	**5,262,000**	–
3–4 years	**5,262,000**	–
4–5 years	**303,231,467**	–
5–10 years	**680,000,000**	680,000,000
More than 10 years	**50,000,000**	50,000,000
Total	**$ 1,046,386,467**	$ 730,000,000

7. Equity

Subscribed Capital

At December 31, 2013 and 2012, the Bank had authorized and subscribed 300,000 shares of capital stock, with a par value of $10,000 per share. As defined in the Charter, capital is classified as callable or paid-in at December 31, 2013 and 2012 as follows:

	Mexico		United States		Total	
	Shares	Dollars	Shares	Dollars	Shares	Dollars
Subscribed capital	150,000	$ 1,500,000,000	150,000	$ 1,500,000,000	300,000	$ 3,000,000,000
Less callable subscribed capital	(127,500)	(1,275,000,000)	(127,500)	(1,275,000,000)	(255,000)	(2,550,000,000)
Paid-in capital	22,500	225,000,000	22,500	225,000,000	45,000	450,000,000
Less transfer to General Reserve for Domestic Programs	–	(22,500,000)	–	(22,500,000)	–	(45,000,000)
Total funded paid-in capital	22,500	$ 202,500,000	22,500	$ 202,500,000	45,000	$ 405,000,000

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 2013	December 31 2012
Designated retained earnings		
International Program:		
Water Conservation Investment Fund (WCIF):		
United States	**$ 3,819,357**	$ 5,319,985
Mexico	**–**	9,593
Total WCIF	**3,819,357**	5,329,578
Technical Assistance Program (TAP)	**5,284,984**	5,546,031
Community Assistance Program (CAP)	**11,473,415**	10,418,219
Total International Program	**20,577,756**	21,293,828
U.S. Domestic Program	**(914,068)**	(696,572)
Total designated retained earnings	**19,663,688**	20,597,256
Reserved retained earnings		
International Program:		
Debt Service Reserve	**18,431,594**	12,844,685
Operating Expenses Reserve	**9,375,607**	8,736,580
Special Reserve	**30,000,000**	27,297,602
Capital Preservation Reserve	**27,298,802**	20,910,150
Total International Program	**85,106,003**	69,789,017
U.S. Domestic Program:		
Special Reserve	**34,667**	45,214
Total reserved retained earnings	**85,140,670**	69,834,231
Undesignated retained earnings		
International Program	**16,013,735**	23,393,315
Total undesignated retained earnings	**16,013,735**	23,393,315
Total retained earnings	**$ 120,818,093**	$ 113,824,802
Retained earnings by program		
International Program	**$ 121,697,494**	$ 114,476,160
U.S. Domestic Program	**(879,401)**	(651,358)
Total retained earnings	**$ 120,818,093**	$ 113,824,802

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

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, 2013 and 2012:

	December 31, 2013		
	Beginning Balance	**Period Activity**	**Ending Balance**
Unrealized gain (loss) on available-for-sale investment securities	**$ 385,530**	**$ (1,156,789)**	**$ (771,259)**
Foreign currency translation adjustment	**59,935**	**(41,184)**	**18,751**
Unrealized gain (loss) on hedging activities:			
Foreign currency translation adjustment	**(15,582,990)**	**(5,532)**	**(15,588,522)**
Fair value of cross-currency interest rate swaps	**17,502,536**	**(9,211,861)**	**8,290,675**
Net unrealized gain (loss) on hedging activities	**1,919,546**	**(9,217,393)**	**(7,297,847)**
Total accumulated other comprehensive income (loss)	**$ 2,365,011**	**$ (10,415,366)**	**$ (8,050,355)**

	December 31, 2012		
	Beginning Balance	**Period Activity**	**Ending Balance**
Unrealized gain (loss) on available-for-sale investment securities	$ 2,382,536	$ (1,997,006)	$ 385,530
Foreign currency translation adjustment	89,807	(29,872)	59,935
Unrealized gain (loss) on hedging activities:			
Foreign currency translation adjustment	(33,700,100)	18,117,110	(15,582,990)
Fair value of cross-currency interest rate swaps	51,962,035	(34,459,499)	17,502,536
Net unrealized gain (loss) on hedging activities	18,261,935	(16,342,389)	1,919,546
Total accumulated other comprehensive income (loss)	$ 20,734,278	$ (18,369,267)	$ 2,365,011

8. Domestic Programs

As specified in the Charter, 10% of each country's paid-in capital is to be set aside to finance community adjustment and investment programs in support of the purposes of NAFTA. In accordance with the Charter, the Board of Directors approved transfers in prior years of $45,000,000, equal to 10% of paid-in capital of $450,000,000, 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 indicates that 10% of paid-in capital from Mexico and the related earnings be set aside for the community adjustment and investment program endorsed by Mexico. The Mexican federal government instituted its domestic program, titled *Programa Complementario de Apoyo a Comunidades y Empresas* (Mexican Domestic Program), through the offices of the SHCP. In June 1996, the 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.

8. Domestic Programs (continued)

United States

The MOU with the U.S. government specifies that 10% of the paid-in capital from the United States and the related earnings be set aside for the U.S. Community Adjustment and Investment Program (U.S. Domestic Program). Additionally, the MOU specified that the Los Angeles office of the Bank be formed to administer the U.S. Domestic Program. The Bank provides financing endorsed by the Finance Committee appointed by the U.S. government for that purpose. Upon written endorsement from the U.S. government, U.S. Domestic Program funds can be transferred to the U.S. government. Returns of capital to the U.S. government are reported as a deduction from allocated paid-in capital. During the years ended December 31, 2013 and 2012, no funds were transferred to the U.S. Treasury for U.S. Domestic Program activities.

In accordance with the Charter and MOU with the United States, net assets of the Bank in the amounts of $4,894,188 and $5,951,480 were designated for the U.S. Domestic Program at December 31, 2013 and 2012, respectively. The revenue related to these amounts for the years ended December 31, 2013 and 2012 were $58,104 and $105,355, respectively. Additionally, expenses directly related to the operation of the U.S. Domestic Program of $286,147 and $348,188 are included in the operations of the Bank for the years ended December 31, 2013 and 2012, 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, 2013 and 2012 were $879,401 and $651,358, respectively. Under the U.S. Domestic Program, $3,794,047 in cash and cash equivalents was available for disbursement as of December 31, 2013.

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, 2013 and 2012, the U.S. Domestic Program's allocated paid-in capital totaled $5,773,589 and $6,602,838, respectively. For the years ended December 31, 2013 and 2012, $829,249 and $1,508,879, 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	
	2013	**2012**
Program income:		
EPA grant	**$ 1,207,801**	$ 1,589,277
Total program income	**1,207,801**	1,589,277
Program expenses:		
EPA grant administration	**(1,207,801)**	(1,589,277)
Technical Assistance Program	**(689,865)**	(688,313)
Solid Waste Environmental Program	**–**	(1,050,691)
Water Conservation Investment Fund	**(455,025)**	(698,422)
Total program expenses	**(2,352,691)**	(4,026,703)
Net program expenses	**$ (1,144,890)**	$ (2,437,426)

9. Program Activities (continued)

EPA Grants

The Bank administers grant funds from EPA through the Border Environment Infrastructure Fund (BEIF). EPA grant awards since the initial grant made in April 1997 to December 31, 2013 total $673,230,665. 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, 2013, EPA has approved project funding proposed by the Bank totaling $597,702,434, of which $569,258,527 has been disbursed through the Bank. The Bank recognized $1,207,801 and $1,589,277 as reimbursement of expenses incurred for the years ended December 31, 2013 and 2012, respectively. These funds have been recorded as program revenue and expenses in the consolidated statements of income.

Technical Assistance Program (TAP)

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 for studies related to the design and implementation of environmental infrastructure projects, as well as for capacity-building measures aimed at achieving the effective and efficient operation of public services. For the years ended December 31, 2013 and 2012, $261,047 and $300,983, 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, 2013 and 2012, $428,818 and $387,330, respectively, was expended under this program.

Solid Waste Environmental Program (SWEP)

In October 1999, the Board of Directors approved a grant program for municipal solid waste financing funded with a portion of the Bank's retained earnings. The Board designated a cumulative total of $13,950,000 for the SWEP. For the years ended December 31, 2013 and 2012, $0 and $1,050,691, respectively, was disbursed under this program. These disbursements were funded with previously designated retained earnings and have been reported as a program expense.

In February 2011, the Board agreed to consolidate the Bank's grant financing activity funded from its retained earnings under a single program, thereby replacing the SWEP. The final SWEP disbursement was made in December 2012 for a cumulative program total of $9,882,756. A cumulative total of $4,067,244 in uncommitted SWEP funds was rolled over to the Community Assistance Program (CAP) as of December 31, 2012.

Water Conservation Investment Fund (WCIF)

In August 2002, the Board of Directors established the WCIF program 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 WCIF. Of that amount, $40,000,000 is reserved exclusively for water conservation projects in each country. For the years ended December 31, 2013 and 2012, $455,025 and $698,422 were disbursed under this fund. As of December 31, 2013, cumulative disbursements total $35,135,040 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.

9. Program Activities (continued)

In May 2013, the Board agreed to close out the WCIF and transfer any uncommitted funds to the CAP program. As of December 31, 2013, a cumulative total of $1,055,196 in uncommitted WCIF funds has been rolled over 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, 2013, a cumulative total of $11,473,415 in retained earnings has been allocated to the CAP, including $4,067,244 and $1,055,196 in uncommitted funds that were rolled over from the SWEP and WCIF, respectively. For the years ended December 31, 2013 and 2012, no funds were disbursed under this program.

10. 401(a) Retirement Plan

The Bank has a 401(a) Retirement Plan (the Plan) for its employees. The Plan provides for employee and nondiscretionary employer contributions. For the years ended December 31, 2013 and 2012, the Bank expended $587,750 and $600,962, respectively, relating to the Plan.

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 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, in its understanding, 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 discounted cash flow analyses, using 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.

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 market cross-currency swaps are all Mexican-peso for U.S.-dollar operations. Mexican-peso

11. Fair Value of Financial Instruments (continued)

cash flows are discounted using the Mexico Benchmark Interbank Deposit Rate (TIIE) 28-day swap curve. U.S.-dollar cash flows are discounted using the 3-month London Interbank Offered Rate (LIBOR) swap curve.

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 benchmark 3-month LIBOR swap curve, as well as external pricing models and counterparty pricing.

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 external pricing models and counterparty pricing. Mexican-peso cash flows are discounted using the TIIE 28-day swap curve. U.S.-dollar cash flows are discounted using the 3-month LIBOR swap curve.

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 benchmark 3-month LIBOR swap curve, as well as external pricing models and counterparty pricing.

Long-term Debt and Accrued Interest Payable
The long-term debt is carried at amortized cost. The fair value of the long-term debt is estimated by discounting the cash flow stream using the benchmark swap curve. The carrying amount of accrued interest payable approximates its fair value.

The carrying amounts and fair value of the Bank's financial instruments are as follows:

	December 31, 2013		December 31, 2012	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Assets				
Cash and cash equivalents	**$ 60,604,326**	**$ 60,604,326**	$ 66,890,985	$ 66,890,985
Held-to-maturity securities	**53,619,703**	**59,177,603**	53,593,008	63,532,006
Available-for-sale securities	**435,095,011**	**435,095,011**	272,623,600	272,623,600
Loans, net	**962,798,909**	**964,294,826**	861,197,880	894,436,518
Interest receivable	**10,331,837**	**10,331,837**	8,515,615	8,515,615
Cross-currency interest rate swaps	**20,059,058**	**20,059,058**	22,321,693	22,321,693
Interest rate swaps	**26,962,548**	**26,962,548**	31,817,912	31,817,912
Liabilities				
Accrued interest payable	**8,343,188**	**8,343,188**	6,664,697	6,664,697
Cross-currency interest rate swaps	**6,606,616**	**6,606,616**	7,697,783	7,697,783
Interest rate swaps	**50,763,499**	**50,763,499**	11,417,251	11,417,251
Long-term debt, net	**1,041,314,034**	**1,003,770,775**	724,975,593	753,380,062

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, 2013 and 2012, 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.

	December 31, 2013			
	Fair Value Measurements Using			
	Level 1	Level 2	Level 3	Total Fair Value
Assets				
Available-for-sale (AFS) securities:				
U.S. government securities	$ 176,805,681	$ –	$ –	$ 176,805,681
U.S. agency securities	–	92,281,412	–	92,281,412
Corporate debt securities	–	104,601,368	–	104,601,368
Other fixed-income securities	–	42,955,204	–	42,955,204
Mexican government securities (UMS)	–	18,372,500	–	18,372,500
Mortgage-backed securities	–	78,846	–	78,846
Total AFS securities	176,805,681	258,289,330	–	435,095,011
Cross-currency interest rate swaps	–	–	20,059,058	20,059,058
Interest rate swaps	–	–	26,962,548	26,962,548
Hedged items for loans	–	–	(17,343,992)	(17,343,992)
Total assets at fair value	$ 176,805,681	$ 258,289,330	$ 29,677,614	$ 464,772,625
Liabilities				
Cross-currency interest rate swaps	$ –	$ –	$ 6,606,616	$ 6,606,616
Interest rate swaps	–	–	50,763,499	50,763,499
Hedged item for notes payable	–	–	(34,189,989)	(34,189,989)
Total liabilities at fair value	$ –	$ –	$ 23,180,126	$ 23,180,126

11. Fair Value of Financial Instruments (continued)

	December 31, 2012			
	Fair Value Measurements Using			
	Level 1	Level 2	Level 3	Total Fair Value
Assets				
Available-for-sale (AFS) securities:				
U.S. government securities	$ 116,193,804	$ –	$ –	$ 116,193,804
U.S. agency securities	–	44,743,856	–	44,743,856
Corporate debt securities	–	63,674,891	–	63,674,891
Other fixed-income securities	–	26,840,635	–	26,840,635
Mexican government securities (UMS)	–	20,830,000	–	20,830,000
Mortgage-backed securities	–	340,414	–	340,414
Total AFS securities	116,193,804	156,429,796	–	272,623,600
Cross-currency interest rate swaps	–	–	22,321,693	22,321,693
Interest rate swaps	–	–	31,817,912	31,817,912
Hedged items for loans	–	–	9,451,273	9,451,273
Total assets at fair value	$ 116,193,804	$ 156,429,796	$ 63,590,878	$ 336,214,478
Liabilities				
Cross-currency interest rate swaps	$ –	$ –	$ 7,697,783	$ 7,697,783
Interest rate swaps	–	–	11,417,251	11,417,251
Hedged item for notes payable	–	–	28,404,469	28,404,469
Total liabilities at fair value	$ –	$ –	$ 47,519,503	$ 47,519,503

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, 2013 and 2012. 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, 2013	$ 22,321,693	$ 31,817,912	$ 9,451,273
Total realized and unrealized gains (losses):			
Included in earnings (expenses)	**(621,786)**	**(4,855,364)**	**(26,795,265)**
Included in other comprehensive income (loss)	**(1,640,849)**	**–**	**–**
Purchases	**–**	**–**	**–**
Settlements	**–**	**–**	**–**
Transfers in/out of Level 3	**–**	**–**	**–**
Ending balance, December 31, 2013	**$ 20,059,058**	**$ 26,962,548**	**$ (17,343,992)**
Beginning balance, January 1, 2012	$ 58,554,240	$ 20,035,019	$ 2,475,377
Total realized and unrealized gains (losses):			
Included in earnings (expenses)	(7,923,744)	11,782,893	6,975,896
Included in other comprehensive income (loss)	(28,308,803)	–	–
Purchases	–	–	–
Settlements	–	–	–
Transfers in/out of Level 3	–	–	–
Ending balance, December 31, 2012	$ 22,321,693	$ 31,817,912	$ 9,451,273
Liabilities			
Beginning balance, January 1, 2013	$ 7,697,783	$ 11,417,251	$ 28,404,469
Total realized and unrealized (gains) losses:			
Included in (earnings) expenses	**(8,662,178)**	**39,346,248**	**(62,594,458)**
Included in other comprehensive (income) loss	**7,571,011**	–	–
Purchases	–	–	–
Settlements	–	–	–
Transfers in/out of Level 3	–	–	–
Ending balance, December 31, 2013	**$ 6,606,616**	**$ 50,763,499**	**$ (34,189,989)**
Beginning balance, January 1, 2012	$ –	$ –	$ 28,032,512
Total realized and unrealized (gains) losses:			
Included in (earnings) expenses	1,547,087	11,417,251	371,957
Included in other comprehensive (income) loss	6,150,696	–	–
Purchases	–	–	–
Settlements	–	–	–
Transfers in/out of Level 3	–	–	–
Ending balance, December 31, 2012	$ 7,697,783	$ 11,417,251	$ 28,404,469

11. Fair Value of Financial Instruments (continued)

The Bank entered into 15 cross-currency interest rate swaps and four interest rate swaps during the year ended December 31, 2013. Upon issuance, the fair value of the swaps is $0 and, therefore, is not portrayed in the purchases and settlements line item above. The change in fair value of these instruments is included within the total gains (losses) line item above.

Impaired loans are reported at the fair value of the underlying collateral if repayment is expected solely from the collateral. The impaired loans are reported at fair value through a specific valuation allowance allocation of the allowance for loan losses. Collateral values are estimated using Level 3 inputs based on customized valuation procedures. As of December 31, 2013, one impaired loan with a carrying value of $3,441,055 has been reduced by specific valuation allowance allocations totaling $3,441,055 to a total reported fair value of $0 based on collateral valuations using Level 3 inputs.

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. In March 2012, the Bank foreclosed on the collateral of one loan under the International Program with a net asset value of $800,000. During October 2012 and February 2013, a portion of this collateral was sold for cash for $146,693. In December 2013, the Bank foreclosed on a loan under the International Program and received as partial payment collateral with a net asset value of $7,179,731. The collateral from the foreclosed loans is reported as other assets of $7,833,038 as of December 31, 2013. For the year ended December 31, 2013, the Bank did not remeasure any existing real estate owned and did not record any impairment on 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 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 decrease over time to match the expected amortization of the underlying loan.

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.

12. Derivative Financial Instruments (continued)

Neither the Bank nor the counterparty is required to post collateral to support the outstanding fair value of the swaps under its arrangement with FOAEM. 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 $4,800,000 and $14,500,000 was posted from a counterparty to the Bank as of December 31, 2013 and 2012, respectively. Cash collateral of $19,720,000 and $0 was posted by the Bank as of December 31, 2013 and 2012, respectively.

The notional amounts and estimated fair values of the swaps outstanding at December 31, 2013 and 2012 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, 2013		December 31, 2012	
	Notional Amount	**Estimated Fair Value**	**Notional Amount**	**Estimated Fair Value**
Cross-currency interest rate swaps	**$ 339,577,373**	**$ 14,560,033**	$ 321,655,401	$ 14,954,314
Interest rate swaps	**1,190,487,286**	**(23,800,951)**	825,071,799	20,400,661

The referenced exchange rate received for the cross-currency interest rate swaps outstanding at December 31, 2013 and 2012 was 7.67% and 7.78%, respectively.

Swaps that are no longer deemed effective because of borrower default on the hedged loans are not included in the table above. The fair value of these swaps was $(1,107,591) and $(330,404) as of December 31, 2013 and 2012, respectively.

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 other income or expense. 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 $(7,297,847) and $1,919,547 at December 31, 2013 and 2012, 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 other income or expense. For the years ended December 31, 2013 and 2012, changes in the aforementioned swaps were $(868,552) and $(2,951,135), 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 exactly offset the changes in the fair value of the loans and debt due to changes in the LIBOR swap rate; therefore, there is no impact to the consolidated statements of income for the period. The fair value of the interest rate swaps was reported as other assets of $26,962,548 and other liabilities of $50,763,499 at December 31, 2013 and as other assets of $31,817,912 and other liabilities of $11,417,251 at December 31, 2012 in the accompanying consolidated balance sheets.

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, 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 loan receivables disclosed in Note 4 and the long-term borrowings disclosed in Note 6. Under agreements with consultants and contractors in effect at December 31, 2013, 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, are not recorded in the financial statements.

15. Accounting Standards Updates

Accounting Standards Update (ASU) No. 2011-05, *Comprehensive Income (Topic 220) – Presentation of Comprehensive Income*. ASU No. 2011-05 amends Topic 220, *Comprehensive Income*, to require that all non-owner changes in stockholders' equity be presented in either a single continuous statement of comprehensive income or in two separate but consecutive statements. Additionally, ASU No. 2011-05 requires entities to present, on the face of the financial statements, reclassification adjustments for items that are reclassified from other comprehensive income to net income in the statement or statements where the components of net income and the components of other comprehensive income are presented. The option to present components of other comprehensive income as part of the statement of changes in stockholders' equity was eliminated. ASU No. 2011-05 is effective for fiscal years ending after December 15, 2012, and interim and annual periods thereafter; however, certain provisions related to the presentation of reclassification adjustments have been deferred by ASU No. 2011-12, *Comprehensive Income (Topic 220) – Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in ASU No. 2011-05*, as further discussed below. The required disclosures are reported herein with no significant impact to the consolidated financial statements.

ASU No. 2011-11, *Balance Sheet (Topic 210) – Disclosures about Offsetting Assets and Liabilities*. ASU No. 2011-11 amends Topic 210, *Balance Sheet*, to require an entity to disclose both gross and net information about financial instruments, such as sales and repurchase agreements and reverse sale and repurchase agreements and securities borrowing/lending arrangements, and derivative instruments that are eligible for offset in the balance sheet and/or subject to a master netting arrangement or similar agreement. ASU No. 2011-11 is effective for annual and interim periods beginning on January 1, 2013, and the required disclosures are reported herein with no significant impact to the consolidated financial statements.

ASU No. 2013-02, *Comprehensive Income (Topic 220) – Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income.* ASU 2013-02 amends recent guidance related to the reporting of comprehensive income to enhance the reporting of reclassification out of accumulated other comprehensive income. ASU 2013-02 became effective for the Bank on January 1, 2013 and did not have a significant impact on the Bank's consolidated financial statements.

15. Accounting Standards Updates (continued)

ASU 2013-10, *Derivatives and Hedging (Topic 815) – Inclusion of the Fed Funds Effective Swap Rate (or Overnight Index Swap Rate) as a Benchmark Interest Rate for Hedge Accounting Purposes*. ASU 2013-10 permits the Fed Funds Effective Swap Rate (or Overnight Index Swap Rate) to be used as a U.S. benchmark interest rate for hedge accounting purposes under Topic 815, in addition to interest rates on direct Treasury obligations of the U.S. government and the London Interbank Offered Rate (LIBOR). ASU 2013-10 is effective for qualifying new or re-designated hedging relationships entered into on or after July 17, 2013 and did not have a significant impact to the Bank's consolidated financial statements.

16. Subsequent Events

The Bank has evaluated subsequent events for potential recognition and/or disclosure through March 31, 2013, the date these consolidated financial statements were issued.

Supplementary Information

Combining Balance Sheet by Program

December 31, 2013

	International Program	U.S. Domestic Program (A)	Eliminations	Total
Assets				
Cash and cash equivalents:				
Held at other financial institutions in demand deposit accounts	$ 74,454	$ 1,894	$ –	$ 76,348
Held at other financial institutions in interest bearing accounts	39,335,825	192,153	–	39,527,978
Repurchase agreements	17,400,000	3,600,000	–	21,000,000
	56,810,279	3,794,047	–	60,604,326
Held-to-maturity investment securities, at amortized cost	53,619,703	–	–	53,619,703
Available-for-sale investment securities, at fair value	435,095,011	–	–	435,095,011
Loans outstanding	1,011,211,596	1,155,568	–	1,012,367,164
Allowance for loan losses	(12,894,119)	(23,188)	–	(12,917,307)
Unamortized loan fees	(3,411,490)	–	–	(3,411,490)
Foreign currency exchange rate adjustment	(16,054,882)	–	–	(16,054,882)
Hedged items, at fair value	(17,343,992)	–	–	(17,343,992)
Net loans outstanding	961,507,113	1,132,380	–	962,639,493
Interest receivable	10,328,351	3,486	–	10,331,837
Grant and other receivable	419,481	–	–	419,481
Due from U.S. Domestic Program	26,014	–	(26,014)	–
Furniture, equipment and leasehold improvements, net	190,875	2,075	–	192,950
Other assets	55,079,144	–	–	55,079,144
Total assets	$ 1,573,075,971	$ 4,931,988	$ (26,014)	$ 1,577,981,945
Liabilities and equity				
Liabilities:				
Accounts payable	$ 993,536	$ –	$ –	$ 993,536
Accrued liabilities	310,570	11,786	–	322,356
Due to International Program	–	26,014	(26,014)	–
Accrued interest payable	8,343,188	–	–	8,343,188
Undisbursed grant funds	1,005	–	–	1,005
Other liabilities	37,650,115	–	–	37,650,115
Long-term debt, net of discount	1,041,314,034	–	–	1,041,314,034
Hedged items, at fair value	(34,189,989)	–	–	(34,189,989)
Long-term debt, net	1,007,124,045	–	–	1,007,124,045
Total liabilities	1,054,422,459	37,800	(26,014)	1,054,434,245
Equity:				
Paid-in capital	405,000,000	–	–	405,000,000
General Reserve:				
Allocated paid-in capital	–	5,773,589	–	5,773,589
Retained earnings:				
Designated	20,577,756	(914,068)	–	19,663,688
Reserved	85,106,003	34,667	–	85,140,670
Undesignated	16,013,735	–	–	16,013,735
Accumulated other comprehensive loss	(8,050,355)	–	–	(8,050,355)
Minority interest	6,373	–	–	6,373
Total equity	518,653,512	4,894,188	–	523,547,700
Total liabilities and equity	$ 1,573,075,971	$ 4,931,988	$ (26,014)	$ 1,577,981,945

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, 2013

	International Program	U.S. Domestic Program (A)	Total
Income:			
Interest:			
Investment income	$ 4,393,791	$ 1,573	$ 4,395,364
Loan income	35,149,421	56,531	35,205,952
Loss on sales of available-for-sale investment securities, net	(8,011)	–	(8,011)
Fee income	46,261	–	46,261
Other	100	–	100
Total revenues	39,581,562	58,104	39,639,666
Operating expenses:			
Personnel	5,193,127	–	5,193,127
Consultants	2,346,345	–	2,346,345
General and administrative	1,049,866	–	1,049,866
Operational travel	281,591	–	281,591
Depreciation and amortization	35,480	–	35,480
Provision for loan losses	10,544,119	–	10,544,119
Other	926,792	–	926,792
U.S. Domestic Program	–	286,147	286,147
Total operating expenses	20,377,320	286,147	20,663,467
Interest expense	10,838,179	–	10,838,179
Income (loss) before program activities	8,366,063	(228,043)	8,138,020
Program activities:			
EPA grant income	1,207,801	–	1,207,801
EPA grant administration	(1,207,801)	–	(1,207,801)
TAP	(689,865)	–	(689,865)
WCIF	(455,025)	–	(455,025)
Net program expenses	(1,144,890)	–	(1,144,890)
Income (loss) before minority interest	7,221,173	(228,043)	6,993,130
Net loss attributable to minority interest	(161)	–	(161)
Net income (loss) attributable to NADB	$ 7,221,334	$ (228,043)	$ 6,993,291
General Reserve, January 1, 2013			
Allocated paid-in capital	$ –	$ 6,602,838	$ 6,602,838
Retained earnings	114,476,160	(651,358)	113,824,802
Current period activity:			
Net income (loss)	7,221,334	(228,043)	6,993,291
TGP disbursements of the U.S. Domestic Program	–	(829,249)	(829,249)
General Reserve, December 31, 2013			
Allocated paid-in capital	–	5,773,589	5,773,589
Retained earnings	121,697,494	(879,401)	120,818,093
	$ 121,697,494	$ 4,894,188	$ 126,591,682

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, 2013

	International Program	U.S. Domestic Program (A)	Total
Net income (loss)	$ 7,221,334	$ (228,043)	$ 6,993,291
Other comprehensive income (loss):			
Available-for-sale investment securities:			
Change in unrealized gains (losses) during the period, net	(1,164,800)	–	(1,164,800)
Reclassification adjustment for net loss included in net income	8,011	–	8,011
Total unrealized loss on available-for-sale investment securities	(1,156,789)	–	(1,156,789)
Foreign currency translation adjustment	(41,184)	–	(41,184)
Unrealized losses on hedging activities:			
Foreign currency translation adjustment, net	(5,532)	–	(5,532)
Fair value of cross-currency interest rate swaps, net	(9,211,861)	–	(9,211,861)
Total unrealized loss on hedging activities	(9,217,393)	–	(9,217,393)
Total other comprehensive loss	(10,415,366)	–	10,415,366
Total comprehensive loss	$ (3,194,032)	$ (228,043)	$ (3,422,075)

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, 2013

	International Program	U.S. Domestic Program (A)	Total
Operating activities			
Net income (loss)	$ 7,221,334	$ (228,043)	$ 6,993,291
Adjustments to reconcile net income (loss) to net cash used in operating activities:			
Depreciation and amortization	35,480	–	35,480
Amortization of net premium on investments	1,980,067	–	1,980,067
Change in fair value of swaps	(26,463,294)	–	(26,463,294)
Minority interest	(161)	–	(161)
Loss on sales of available-for-sale investment securities, net	8,011	–	8,011
Provision for loan losses	10,544,119	–	10,544,119
Change in other assets and liabilities:			
Increase in interest receivable	(1,815,914)	(308)	(1,816,222)
Increase in receivable and other assets	(7,605,846)	–	(7,605,846)
Decrease in due from U.S. Domestic Program due to International Program	32,329	(32,329)	–
Decrease in accounts payable	(75,706)	–	(75,706)
Increase in accrued liabilities	84,087	660	84,747
Increase in accrued interest payable	1,678,491	–	1,678,491
Net cash used in operating activities	(14,377,003)	(260,020)	(14,637,023)
Lending, investing, and development activities			
Capital expenditures	(91,331)	(2,075)	(93,406)
Loan principal repayments	73,733,283	351,585	74,084,868
Loan disbursements	(214,964,344)	–	(214,964,344)
Purchase of held-to-maturity investments	(1,150,000)	–	(1,150,000)
Purchase of available-for-sale investments	(558,724,883)	–	(558,724,883)
Proceeds from maturities of held-to-maturity investments	1,145,000	–	1,145,000
Proceeds from sales and maturities of available-for-sale investments	393,086,910	–	393,086,910
Net cash provided by (used in) lending, investing, and development activities	(306,965,365)	349,510	(306,615,855)
Financing activities			
Proceeds from other borrowings	16,386,468	–	16,386,468
Proceeds from note issuance	299,409,000	–	299,409,000
Grant funds –- EPA	18,976,292	–	18,976,292
Grant disbursements – EPA	(18,976,292)	–	(18,976,292)
Grant activity – U.S. Domestic Program	–	(829,249)	(829,249)
Net cash provided by (used in) financing activities	315,795,468	(829,249)	314,966,219
Net decrease in cash and cash equivalents	(5,546,900)	(739,759)	(6,286,659)
Cash and cash equivalents at January 1, 2013	62,357,179	4,533,806	66,890,985
Cash and cash equivalents at December 31, 2013	$ 56,810,279	$ 3,794,047	$ 60,604,326

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

Border Environment Infrastructure Fund (BEIF)

As of and for the Year Ended December 31, 2013

Balance Sheet

	Region 6	Region 9	Total
Assets			
Cash	$ 501	$ 504	$ 1,005
Total assets	$ 501	$ 504	$ 1,005
Liabilities			
Undisbursed grant funds	$ 501	$ 504	$ 1,005
Total liabilities	$ 501	$ 504	$ 1,005

Statement of Income

	Region 6	Region 9	Total
Income:			
U.S. Environmental Protection Agency grant income	$ 587,300	$ 620,501	$ 1,207,801
Total income	587,300	620,501	1,207,801
BEIF operating expenses:			
Personnel	341,181	326,156	667,337
Consultants	159,345	219,532	378,877
General and administrative	72,194	48,123	120,317
Operational travel	14,580	26,690	41,270
Total BEIF operating expenses	587,300	620,501	1,207,801
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	15,701,842	3,274,450	18,976,292
Grant disbursements – EPA	(15,701,842)	(3,274,450)	(18,976,292)
Net cash provided by financing activities	–	–	–
Net increase in cash and cash equivalents	–	–	–
Cash and cash equivalents at January 1, 2013	501	504	1,005
Cash and cash equivalents at December 31, 2013	$ 501	$ 504	$ 1,005

Region 6: EPA Regional Office located in Dallas, Texas

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

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