# ANNUAL REPORT
# 2005

# Content

Corporación Andina de Fomento (CAF) is a multilateral financial institution which supports the sustainable development of its shareholder countries and integration efforts within the region. Its shareholders are the five countries of the Andean Community: Bolivia, Colombia, Ecuador, Peru and Venezuela, as well as Argentina, Brazil, Chile, Costa Rica, Dominican Republic, Jamaica, Mexico, Panama, Paraguay, Spain, Trinidad & Tobago, Uruguay and 16 private banks in the region.

CAF serves both the public and private sectors by providing multiple financial services to a broad customer base comprised of shareholder countries, corporations and financial institutions. Its management policies incorporate social and environmental variables, and its operations include ecoefficiency and sustainability criteria. As a financial intermediary it attracts resources from industrialized countries to Latin America, and serves as a bridge between international capital markets and the region by promoting investments and business opportunities.

## Financial highlights in 2005

- Total assets: US$ 9,540 million (US$ 9,586 million in 2004)
- Liquid assets: US$ 1,788 million (US$ 1,727 million in 2004)
- Loan and investment portfolio: US$ 7,462 million (US$ 7,216 million in 2004)
- Pain-in capital: US$ 1,682 million (US$ 1,499 million in 2004)
- Shareholder's equity: US$ 3,237 million (US$ 2,793 million in 2004)
- Net profit: US$ 283 million (US$ 208 million in 2004)

### CAF's most relevant accomplishments in 2005:

- Marking its 35th anniversary as a strong, competitive and internationally renowned Latin American institution, which has become the main source of multilateral financing for the Andean countries, while emphasizing its support for sustainable development in its shareholder countries, and playing a leading role in the region's integration process.
- Supporting the dynamic expansion of the region's economies with record approvals of US$ 4,746 million, including nearly one billion dollars for integration-related infrastructure projects –particularly in South America– and over 1,900 million dollars to support private investment in shareholder countries, while reinforcing its catalytic role through innovative products and services.
- Earmarking US$ 32 million in non-reimbursable resources for community, cultural and social development activities, as well as for governance, competitiveness, and environmental programs, and to support SMEs and Microfinance, while promoting new mechanisms for sectors with limited access to capital.
- Achieving strong financial results, with sustained growth in all its indicators and attaining an unprecedented level of net profits amounting to US$ 283 million. CAF also improved its excellent investment credit ratings by obtaining, for the first time, a *AA*- rating by the Japan Credit Rating Agency.
- Having the Shareholders' Assembly approve a reform of its Constitutive Agreement, in order to allow non-Andean shareholders and other countries of the region to attain full membership.
- Fostering public debate and disseminating information on economic, social and environmental issues in Latin America, with a view to promoting a renewed development agenda for the region.

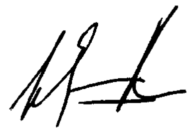
## Letter from the Executive President

I AM PLEASED TO PRESENT the Annual Report and audited financial statements for fiscal year 2005.

In 2005, Latin America once again exhibited a positive macroeconomic performance, partially as a result of favorable international conditions and the resumption of foreign capital flows. These conditions provided an opportunity for the region to consolidate microeconomic structural reforms, in order to ensure sustainable economic growth, greater social inclusion and poverty reduction in the longer term.

In this context, CAF supported its member countries in activities aimed at improving competitiveness and consolidating integration, especially in South America. It also expanded activities in the area of sustainable human development, with a view to improving social equity and inclusion, as well as democratic governance in the region. CAF's efforts are evidenced by its record amount of loan approvals, and by the progress of its strategic programs in implementing a renewed agenda for regional development.

CAF also celebrated its thirty-fifth Anniversary this year with operational and financial results that were highly commended by the shareholders, and boosted the confidence of its clients and international financial partners. These achievements result from the continued support afforded by CAF's shareholders and Board of Directors, and the collective efforts of its staff. To all of them I wish to express my gratitude.



L. Enrique García
President & CEO

# The economic context and regional integration

A POSITIVE ECONOMIC TREND CONTINUED in Latin America during 2005 as the region grew 4.6% with moderate inflation of 6.9%. An export boom, attributed to a favorable external environment, accounts for the region's surplus in the current account of the balance of payments. In turn, external capital flows (especially FDI) returned to the region, although to a lesser extent than during the 1990s. In spite of the rise in international interest rates, country risk levels in Latin America have continued decreasing. This is the result of sound economic fundamentals, a healthy external position, robust financial systems and disciplined macroeconomic management. In general, fiscal policies have been prudent, monetary policies have been independent and effective, and cautious banking regulation has improved banking balances in the financial sector.

The dynamic growth of exports (more than 15%) responds to both an increase in the prices of the main export goods –which reached historic peaks in many cases– and greater export volumes. The external environment has been very favorable for the region, especially due to high primary good demand from emerging economies, like China, and a larger participation of non-traditional Latin American exports in the markets of its main trade partners under preferential agreements.

Notwithstanding these positive aspects, the region continues facing many important challenges. In the first place, Latin America remains vulnerable to changes in the external environment. Second,

**Main indicators of the region**

| | ANDEAN COUNTRIES | | | LATIN AMERICA | | |
|---|---|---|---|---|---|---|
| | 2003 | 2004 | 2005* | 2003 | 2004 | 2005* |
| **Real Sector** | | | | | | |
| GDP (current millions US$) | 258,300 | 332,946 | 387,713 | 1,705,145 | 1,956,244 | 2,372,692 |
| Real GDP Growth (%) | -0.1 | 9.1 | 6.7 | 1.9 | 6.2 | 4.6 |
| Saving (% of GDP) | 19.1 | 21.3 | 23.3 | 19.9 | 21.6 | 24.1 |
| Investment (% of GDP) | 16.4 | 17.2 | 20.1 | 19.1 | 19.9 | 18.6 |
| Unemployment (%) | 13.6 | 11.1 | 10.5 | 10.4 | 9.1 | 8.6 |
| Population (Millions) | 119.1 | 122.1 | 122.2 | 481.1 | 493.4 | 500.1 |
| **External Sector** | | | | | | |
| Exports FOB (millions US$) | 57,716 | 78,667 | 106,311 | 373,672 | 460,551 | 552,596 |
| excluding Venezuela | 29,668 | 39,919 | 50,714 | 345,624 | 421,803 | 496,999 |
| Imports FOB (millions US$) | 39,116 | 49,905 | 68,277 | 326,793 | 371,732 | 466,255 |
| Trade Balance (millions US$) | 18,600 | 28,762 | 29,899 | 46,880 | 88,819 | 66,699 |
| excluding Venezuela | 893 | 5,514 | 3,108 | 29,173 | 65,571 | 39,908 |
| Current Account (% of GDP) | 2.70 | 3.35 | 5.86 | 1.50 | 1.47 | 1.68 |
| excluding Venezuela | -1.73 | -0.54 | -0.25 | 0.96 | 0.95 | 0.80 |
| Net International Reserves (millions US$) | 43,829 | 52,011 | 63,047 | 190,032 | 213,865 | 244,998 |
| Foreing Direct Investment (% of GDP) | 2.62 | 2.17 | 2.16 | 2.04 | 2.85 | 2.40 |
| Total External Debt (% of GDP) | 41.78 | 37.28 | 30.59 | 54.86 | 46.74 | 32.70 |
| **Fiscal Sector, Prices and Sovereign Risk** | | | | | | |
| Fiscal Balance NFPS (% of GDP) | -1.4 | -1.9 | -0.3 | -2.5 | -1.0 | 2.2 |
| Inflation (%, end of period) | 12.4 | 9.4 | 7.3 | 7.7 | 6.8 | 6.9 |
| Sovereign Bonds Spread (Basic points) 1/ | 484 | 358 | 346 | 1,815 | 1,316 | 743 |

Source: Public Policies and Competitiveness Office, CAF

*** PRELIMINARY DATA**

**1/** The EMBI+ spread is calculated, for CAN with Colombia, Ecuador, Peru and Venezuela, and for Latin America with Argentina, Brazil, Colombia, Ecuador, Mexico, Panama, Peru and Venezuela.

social tensions and polarization persist in some countries due to ongoing structural problems such as poverty, unemployment, unequal income distribution, and social and economic exclusion. Third, there is a risk that social demands may lead to a relaxation of fiscal discipline, especially in an environment of growing public indebtedness (mainly domestic) and the accumulation of larger fiscal contingencies. Finally, a growing competitiveness gap with respect to other regions and recurrent governance crises have deteriorated the business environment.

Productivity has declined in the last four years, eroding part of the gains attained during the 1990s and leaving Latin America as one of the regions with the worst competitiveness indicators in the world. Additionally, improvements in social conditions have become the main priority in the public policy agenda in most countries. This is partly due to the fact that the resources dedicated to social sectors have not necessarily translated into improvements in social indicators.

No major changes in economic trends are expected in 2006. Growth rates will remain close to 4% in a context of macroeconomic stability. Even with an eventual deterioration of the international environment (i.e. the worsening of terms of trade and a slight deceleration of the global economy) the external sector will remain healthy and exports will have a vigorous performance. Additionally, most Latin American countries will continue supplying commodities to expanding economies, like China, and will negotiate a deepening of its trading ties with other countries. Both these factors will enable a continuation of an export boom.

It is important to highlight that a significant number of countries in the region will undergo electoral processes this year, possibly redefining new political scenarios. Although these processes are positive as they strenghthen the bases of democratic governance, they may defer investment decisions until economic policy changes are defined. It is for this reason that the establishment of long-term policies, with the support of ample consensus within countries, is necessary to ensure policy continuity.

In general, the region continues to have a window of opportunity to carry out an agenda of pending reforms to maintain long-term quality economic growth, that is inclusive and participatory, and to address the social challenges that it still faces. This is particularly important given the upcoming political transitions and the probability that the international environment may become less favorable in the near future.

## International environment

The external environment has been favorable for both Latin America and most emerging economies. Strong growth of the largest world economies has been maintained in a context of low inflation. Chinese strong growth should be viewed with optimism by productive sectors in most economies. Moreover, increasing capital flows –particularly foreign direct investment– should allow for a better use of savings, translating into greater global efficiency.

Nevertheless, the global economic environment may deteriorate. One of the main sources of concern is associated with the historic peaks reached by oil prices (in nominal terms). The low short-term demand elasticity of petroleum has supposed an increase in prices, which raises the risk of global growth slowdown. This, combined with uncertainty of international terrorism, reduces the confidence of economic agents and, therefore, may negatively affect consumption and investment trends worldwide. Another cause for concern has to do with the global imbalances derived from large deficits in the current and fiscal accounts in the US. Its financing could be compromised in the event that capital flows cease to be driven by the increase of productivity and/or if Asian countries decide to change the composition of their international reserves.

Growth in the US economy was 3.7% in 2005. This performance was affected by damages caused by hurricane Katrina, which had a short-term negative impact but no permanent consequences on out-

**In 2005, conditions on the international scene were favorable for the economies of Latin America and emerging markets, with the resumption of foreign capital flows**

put. For 2006, moderate growth is expected due to higher interest rates seeking to contain inflationary pressures, the probable reduction in private consumption in response to high household indebtedness, a possible fall of the real estate market, a slowdown in productivity growth and higher production costs associated to high fuel prices, among others.

Europe grew at a rate close to a third of the United States' in 2005. Unemployment continued to be structurally high and fiscal problems persisted. The euro has lagged behind the US dollar and interest rates have remained low, reaching historical lows in real terms. The accession of new countries to the EU and the defeat of the referendum of the European constitution in France and the Netherlands do not seem to have had significant economic impacts, although envisage important political changes in the future. In spite of recent low growth rates, Germany potentially has the best outlook, given its labor market reforms and expected productivity gains.

**Spain,** a member country of CAF, continued its positive growth trend with a GDP expansion of 3.5% in 2005, slightly higher than the 3.1% experienced in 2004. This performance was influenced by high internal demand growth, which neared 5%. On the other hand, inflation reached 3.4%, somewhat above the goal established by monetary authorities and the one experienced the previous year (3.2%). This result is explained by oil and food price hikes.

Japan exhibited a moderate expansion in 2005 (1.6%), after hosting its best growth rate in several years in 2004. Nevertheless, the Japanese economy is in a better position given the improvement of financial sector balances and the large profits reported by many firms. Besides, it is foreseen that new privatizations and greater economic liberalization will give it a greater dynamism. China, in turn, ended 2005 with a GDP growth rate of 9.5%. This expansion was achieved despite government policies aimed at avoiding economic overheating, by means of higher interest rates and exchange rate revaluation. Furthermore, Chinese trade with the rest of the world continued growing becoming one of the main importers of raw materials and the main destination of FDI in the world.

During 2005 a general increase in world interest rates was posted, and it is expected that this trend will continue in 2006. The Federal Reserve in the US has continued its policy of increasing its short-term interest rates. It is argued that in spite of a possible slowdown in US economic growth, the risk of higher inflation, as a result of high fuel prices, has greater importance. Other central banks have also given indications that they will adopt more restrictive monetary policies. Regarding the global financial system, it is worth noting that it has strengthened in recent years, prompted by considerable improvements in the balance sheets of corporate and financial sectors in most countries. As a consequence, the capacity to absorb potential financial shocks has improved. With expected world growth rates, inflation under control and a relatively benign financial environment, it seems that capital markets will remain sound.

High global liquidity and low returns in industrialized countries have encouraged investors to look toward emerging markets in their search for better returns. Besides, many institutional investors have carried out strategic investments in developing countries, increasing the importance of this type of investments in their portfolio. In spite of the turmoil in corporate debt markets and episodes of political uncertainty in some developing countries in the first half of 2005, market spreads of sovereign bonds have settled within a small range and remained near historic lows.

Regarding commodity markets, oil prices have reached their highest levels since the oil crisis at the end of the seventies, with an average price of US$ 55 per barrel in 2005. The most important factors behind this price hike are an insufficient supply to meet a growing demand (mainly Chinese) and a high dependence on supply from geographical areas that are politically unstable and prone to natural disasters. This has happened in spite of more efficient oil consumption and changes in the energy matrix that have taken place in recent years. Nevertheless, it is expected that the price of oil will moderate in the future as a consequence of lower demand growth rates and higher supply from countries such as Russia and South Africa.

The case of metals is similar; the prices of gold, copper and zinc increased during 2005. The case of agricultural goods, nevertheless, has been varied: while the price of goods such as coffee continued increasing, the price of other goods like soybeans has diminished after having reached historical peaks. This deceleration could also occur to the price of other primary goods if global growth begins to slow down.

## Economic performance

**Argentina** maintained a high growth rate in 2005 (9.2%), explained by a dynamic exporting sector and an expansion of private investment and consumption. Furthermore, after the conclusion of the public debt restructuring with international creditors, balance of payments financing problems were partially corrected. Fiscal accounts showed results in line with the goals set for the year. Nevertheless, it is important not to lose sight of the significant fiscal effort required in the medium term, given a debt balance that continues to represent a high toll on public finances. As a consequence of a combination of factors, such as higher internal demand, the scarce idle installed capacity in certain sectors and public utility hikes, inflation closed at 12.3% in 2005. For 2006 it is foreseen that the Argentinean economy will continue exhibiting a positive trend, although growth will possibly decelerate toward its potential growth level in the medium term.

**As part of their efforts to boost competitiveness, generate jobs and reduce social inequity, the region's countries are making profound changes in their development strategies**

The **Bolivian** economy maintained its course of positive growth during 2005, posting a GDP growth rate of 4.1%. This favorable performance was influenced by an international context in which commodity prices (particularly hydrocarbons) increased considerably, favoring both exports and fiscal accounts. At the same time, private consumption pulled internal demand growth which increased by 3.1%. In the same way, the favorable behavior of consumer prices was reflected in an inflation rate of 4.9%, which implied a deceleration in comparison to the previous year. On the other hand, the performance of the external sector was characterized by a surplus in the current account of the balance of payments larger than the negative balance in the capital and financial accounts, permitting an accumulation of international reserves. In the fiscal sector, partly thanks to new direct hydrocarbon taxes, the government reduced its fiscal deficit to less than 4.5% of GDP in 2005, below the official target of 5.2%.

In the next two years **Brazil** is expected to continue growing moderately, especially due to the dynamism of its exports, higher private consumption, and an improvement in credit conditions. GDP expansion in 2005 was 2.3% and it is expected to be 3.5% in 2006. Exports will continue showing a good performance in the next two years and, although an increase in imports is also expected, the current account of the balance of payments is expected to continue showing a positive balance. In regards to fiscal policy, it is predicted that the government will match or surpass the goals set for the primary surplus during the 2005-2007 period. Thus, the deficit of the consolidated non-financial public sector will continue its downward trend and the public debt to GDP ratio should stabilize around 50%. A reduction of inflationary pressures is expected in 2006, which would bring a loosening of monetary policies, lower interest rates, higher investment and higher output expansion.

In 2005, **Chile's** GDP expanded at a rate of 6.3%. The external sector has been favored mainly by the recovery of copper exports, due to growing Asian demand, especially from China. Nevertheless, the trade surplus has reduced because of the strong import growth associated with the acceleration of domestic demand, and to high oil prices. In the fiscal sector, the government closed the year above the goal set, with a fiscal surplus of 3.4% of GDP. On the other hand, inflation accelerated and closed 2005 at 3.7%, mainly due to high oil prices. It is expected that the economic recovery will consolidate, with GDP growth between 5% and 6% in 2006 and 2007, mainly due to the strengthening of internal demand, both investment and consumption, and to the positive export trend. Risks for the Chilean economy are asso-

**In 2005, almost all shareholder countries posted substantial economic growth within a context of macroeconomic stability and discipline**

ciated to high oil prices, a rise in international interest rates, a possible deceleration of the world economy and uncertainty with respect to the provision of natural gas from Argentina.

**Colombia** grew 4.9% in 2005 and is expected to expand 4.6% in 2006. Growth has been prompted by a very favorable international environment and the improvement in security conditions. It is expected that this trend will continue in the next years. This greater economic expansion has already begun to reflect positively in terms of poverty reduction, and improvements in education, health and employment. The performance of the external sector has been very dynamic. Strong growth in Venezuela and the positive prospects over the signing of a Free Trade Agreement with the United States seem to have compensated in part the competitiveness losses derived from a greater revaluation of the peso. The central bank has tried to control the strengthening of the peso through the purchase of international reserves and the maintenance of historically low interest rates. This has been possible thanks to low inflation rates and the ensuing greater credibility that monetary authorities have achieved. In the fiscal sector, although the general outlook is favorable, an important imbalance in the Central Government accounts exists, although this is partly compensated with the surplus of the decentralized sector.

**Costa Rica** experienced output growth of 4.1% in 2005, a rate similar to the previous year. This expansion was driven by the growth of the manufacturing industry, the farm sector and services, as well as by the dynamism of the exporting sector, especially of high-technology goods. On the other hand, inflation surpassed the set goal of 12.7%, reaching 14.2% due to high oil prices, high agricultural good prices and public utility hikes. In spite of positive economic growth, a marginal increase in open unemployment was registered, going from 6.7% in 2004 to 6.9% in 2005. Regarding the external sector, the current account of the balance of payments posted a deficit slightly over 5.2% of GDP, higher than in 2004.

In 2005 **Ecuador's** GDP increased 3.9% and is expected to expand 2.7% in 2006. A complex social and political outlook led to the postponement of some investment decisions. Nevertheless, poverty rates have remained relatively stable. Inflation has reverted its downward trend given, among other factors, a deterioration of expectations and the strikes that took place in important regions of the country. The trade balance and current account improved substantially given the important increase in oil prices. In the fiscal sector, the non-financial public sector exhibited positive results for the fifth year in a row, thanks to the contribution of social security surplus, higher revenue from oil exports and the upturn in tax collection. Nevertheless, the Central Government's finances sustain a structural deficit of around 1% of GDP. 2006 opens a window of opportunity to debate pending themes and to advance the agenda of structural reforms.

Due to strong ties between **Mexico** and the US, and to high oil prices, the Mexican economy grew 3% in 2005 and is expected to show a similar performance in 2006, although a certain sluggishness in the agricultural sector is foreseen. Nevertheless, the risks are concentrated in the realm of international trade: large technology investments and low costs of certain European countries and China suppose great challenges for Mexican manufacturing exports. In 2005 Mexico posted its lowest inflation since 1969, reaching 3.3%. Revenues originating from oil exports reached more than US$ 27,000 million and the Mexican currency experienced an appreciation of its real exchange rate. The macroeconomic outlook will continue being characterized by moderate growth and low levels of inflation, the moderate loosening of monetary policies in the short-term and low deficits in the external and fiscal accounts.

**Panama** experienced growth of 6.4% in 2005, in good measure fuelled by a positive external environment and internal demand expansion. On a sectoral level, transportation, storage and communications showed the greatest dynamism, followed by commerce and agricultural-fishing, which posted a growth of 6%. Similarly, manufacturing industry showed moderate growth thanks to the expansion of industries related to food processing and metallic good production. In this favorable economic context, urban unemployment decreased from 11.8% to 9.6%. Inflation closed at 4%, a figure that surpassed in 0.6% the rate observed in 2004. Said increment was influenced by the rise in oil prices. With respect to

## Main indicators 2005*

| | Argentina | Bolivia | Brazil | Chile | Colombia |
|---|---|---|---|---|---|
| **Real Sector** | | | | | |
| GDP (current million US$) | 187,587 | 9,707 | 781,562 | 112,180 | 118,642 |
| GDP per capita (current US$) | 4,773.2 | 1,030.0 | 4,211.0 | 6,878.0 | 2,577.0 |
| Real GDP Growth (%) | 9.2 | 4.1 | 2.3 | 6.3 | 4.9 |
| Investment (% of GDP) | 17.4 | 12.1 | 18.4 | 23.2 | 21.0 |
| Unemployment Rate (% of total labor force) | 10.1 | 8.30 | 9.6 | 6.90 | 11.5 |
| Population (millions) | 38.7 | 9.4 | 185.6 | 16.3 | 45.6 |
| **External Sector** | | | | | |
| Exports FOB (millions US$) | 40,013 | 2,671 | 117,700 | 39,536 | 21,187 |
| Imports FOB (millions US$) | 28,692 | 2,341 | 73,487 | 30,300 | 19,779 |
| Current Account (% of GDP) | 1.3 | 4.8 | 1.8 | -0.2 | -1.8 |
| Foreing Direct Investment (% of GDP) | 2.9 | -2.9 | 1.8 | 5.1 | 3.1 |
| Total External Debt (% of GDP) | 75.3 | 73.3 | 24.0 | 9.8 | 19.0 |
| Net International Reserves (millions US$) | 28,077 | 1,714 | 53,574 | 16,963 | 14,721 |
| **Fiscal Sector and Prices** | | | | | |
| Fiscal Balance NFPS (% of GDP) a/ | 1.3 | -1.6 | 4.8 | 4.8 | -1.2 |
| Inflation rate (end of period) | 12.3 | 4.9 | 6.2 | 3.7 | 4.9 |
| Nominal Exchange Rate (end-period) | 3.03 | 8.00 | 2.34 | 512.00 | 2,286.50 |
| Annual Depreciation (%, end-period)) | 2.0 | -0.5 | -12.1 | -7.9 | -2.9 |
| Real Effective Exchange Rate Index (1997=100) | 219.8 | 139.3 | 144.0 | 112.4 | 114.6 |
| **Banking Sector and Capital Markets** | | | | | |
| Nominal Potfolio Growth (%) b/ | 38.9 | 2.5 | n.d. | 14.2 | 10.2 |
| Non-performing Loans (% of Total Loans) | n.d. | 11.3 | n.d. | 0.9 | 3.1 |
| Sovereign Bonds Spread EMBI+ (Basic Pts.) c/ | 2,599 | n.d. | 393 | 80 | 315 |
| Equity Index in US$ (1997=100) d/ | 74.0 | n.d. | 187.8 | 141.4 | 385.0 |
| **Social Indicators*** | | | | | |
| Poverty (% of population) e/ | 28.8 | 63.6 | 37.5 | 18.8 | 49.2 |
| Illiteracy Rate f/ | 2.8 | 13.5 | 11.6 | 4.0 | 5.8 |
| School enrollment, primary (% net) g/ | 100.0 | 95.0 | 96.6 | 99.0 | 87.0 |
| Mortality Infant Rate h/ | 15.0 | 55.6 | 27.3 | 10.3 | 25.6 |
| Life Expentancy at Birth (years) i/ | 74.3 | 63.8 | 71.0 | 75.8 | 72.2 |

*** PRELIMINARY DATA**
a/ Non Financial Public Sector. For Brazil, Dominican Rep. and Uruguay Central Government.
b/ For Argentina data represent Credit to the Private Sector only. Dominican Rep. Data for 2004
c/ Year average. For Chile, Dominican Republic and Uruguay the number presented is EMBI Global.
d/ Data for Uruguay is May 2003=100.
e/ Brazil, Jamaica, Mexico, Panama, Dominican Rep., Trinidad & Tobago and Uruguay data for 2002; Chile data for 2003; Bolivia, Paraguay, Peru and Venezuela data for 2004. Data for Argentina, Costa Rica and Venezuela percentage of household in poverty.
f/ Percent of people ages 15 and above. Data for 2003, except for Paraguay that is for 2004 and Uruguay that is for 2002.
g/ The net enrolment ratio is the ratio of enrolled children of the official age for the education level indicated to the total population of that age. Data for 2003.
h/ Death childs younger than a year, per 1000 live births. Average 2000-2005.
i/ Average 2000-2005.

| Costa Rica | Ecuador | Jamaica | Mexico | Panama | Paraguay | Peru | Dominican Republic | Trinidad & Tobago | Uruguay | Venezuela |
|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | | | | |
| 19,558 | 33,062 | 10,200 | 791,833 | 14,531 | 7,782 | 78,432 | 29,330 | 14,006 | 16,410 | 124,676 |
| 4,520.0 | 2,342 | 3,847.6 | 8,686.4 | 4,496.0 | 1,323.0 | 2,881.5 | 3,247.0 | 10,732.6 | 4,738.7 | 4,661.0 |
| 4.1 | 3.9 | 1.4 | 3.0 | 6.4 | 2.7 | 6.7 | 9.3 | 7.0 | 6.6 | 9.3 |
| 17.1 | 21.5 | n.d. | 18.9 | 17.2 | 15.4 | 18.5 | 17.9 | n.d. | 11.1 | 20.9 |
| 6.90 | 9.30 | 11.50 | 3.53 | 9.60 | 7.30 | 9.60 | 17.00 | 8.20 | 12.10 | 10.50 |
| 4.3 | 13.2 | 2.7 | 107.0 | 3.2 | 6.2 | 27.2 | 9.0 | 1.3 | 3.5 | 26.7 |
| | | | | | | | | | | |
| 7,090 | 9,701 | 1,594 | 213,711 | 6,592 | 1,688 | 17,247 | 5,988 | 8,834 | 3,539 | 55,597 |
| 8,968 | 9,064 | 4,102 | 221,270 | 8,592 | 3,251 | 12,084 | 9,542 | 6,186 | 3,588 | 25,174 |
| -6.8 | -0.2 | -8.8 | -0.4 | -1.5 | -3.7 | 1.3 | -0.8 | 16.4 | -2.8 | 17.7 |
| 3.1 | 4.2 | n.d. | 3.0 | 5.2 | 1.0 | 3.2 | 3.1 | n.d. | 1.9 | 0.4 |
| 30.5 | 47.9 | 69.6 | 15.8 | 60.8 | 29.1 | 36.5 | 22.0 | 21.1 | 68.4 | 30.2 |
| 2,313 | 2,147 | 2,280 | 68,669 | 980 | 1,297 | 14,097 | 1,520 | 3,200 | 3,078 | 30,368 |
| | | | | | | | | | | |
| -2.8 | 0.8 | 0.7 | -0.1 | -3.6 | 0.8 | -0.4 | -0.7 | 3.4 | -2.5 | 0.2 |
| 14.2 | 3.7 | 15.9 | 3.3 | 4.0 | 9.9 | 1.5 | 7.4 | 6.8 | 4.8 | 14.4 |
| 496.65 | 25,000.00 | 64.40 | 10.58 | 1.00 | 6,100.00 | 3.43 | 34.46 | 6.28 | 24.05 | 2,150.00 |
| 8.3 | 0.0 | 5.5 | -4.6 | 0.0 | 0.0 | 4.6 | 20.9 | 1.0 | -8.9 | 12.0 |
| 105.8 | 101.8 | 101.6 | 94.5 | 107.9 | 166.7 | 123.6 | 100.5 | 87.3 | 150.7 | 115.2 |
| | | | | | | | | | | |
| 19.4 | 25.0 | n.d. | 22.0 | n.d. | 13.3 | 16.1 | -6.3 | n.d. | n.d. | 52.9 |
| n.d. | 5.7 | n.d. | 2.5 | n.d. | 5.1 | 2.1 | 7.2 | n.d. | n.d. | 1.0 |
| n.d. | 663 | n.d. | 237 | 266 | n.d. | 202 | 480 | n.d. | 374 | 409 |
| 234.5 | 63.1 | 318.6 | 490.6 | n.d. | n.d. | 212.8 | n.d. | 601.2 | 39.0 | 70.5 |
| | | | | | | | | | | |
| 21.2 | 22.2 | 18.2 | 39.4 | 34.0 | 39.2 | 51.6 | 44.9 | 21.0 | 15.4 | 53.1 |
| 4.2 | 7.8 | 12.4 | 9.7 | 8.1 | 6.4 | 12.3 | 12.3 | 1.5 | 2.3 | 7.0 |
| 90.0 | 100.0 | 94.5 | 99.0 | 100.0 | 89.0 | 100.0 | 96.0 | 91.0 | 90.0 | 98.7 |
| 10.5 | 18.5 | 19.9 | 28.2 | 20.6 | 37.0 | 33.4 | 34.4 | 14.1 | 13.1 | 17.2 |
| 78.1 | 74.0 | 75.7 | 73.4 | 74.7 | 70.8 | 69.8 | 70.1 | 71.3 | 75.2 | 73.0 |

Source: Central Banks, Officials Sources, ECLAC, World Bank and UNDP.

**The region's exports showed impressive growth in 2005 thanks to increases in prices of key export products, with some historic record highs**

foreign trade, the current account deficit increased to 9.8% of GDP, as a result of significant increases in oil and capital good imports.

**Paraguay** registered an economic growth rate of 2.7% in 2005. This expansion was lower than the rate of 4.1% observed in 2004, due to the drought that diminished agricultural production, one of the pillars of the local economy. Nevertheless, exports increased substantially, mainly those of meat products and by products, which increased 73%. Unemployment closed the year at 7.3%, a rate lower than in 2004. In terms of fiscal accounts, there was a fiscal surplus of 0.5% of GDP in 2005, which allowed further public debt reduction. Additionally, inflation closed the year at 9.9%, mainly due to high oil prices. For 2006 the production of soybeans is expected to recover, once the effects of the drought are surpassed. This will positively affect internal output and exports.

For the fourth consecutive year, **Peru** has shown a relatively high growth rate (6.7%), explained mainly by the expansion of exports and higher investment and consumption. The external accounts continue showing highly favorable results. This situation is complemented by a smaller burden of the external public debt service, a result of active liability management carried out by the government. Fiscal accounts show relatively healthy indicators and it is expected that the central bank will not face difficulties in meeting its inflation target in 2006. Forecasts for 2006-07 are favorable. GDP expansion will manage to maintain a rhythm similar to recent years, with growth relatively diversified, both between productive sectors and between internal and external demand. In the fiscal front, it is expected that the government will continue progressing in the reduction of its deficit and public debt, with an orientation toward consolidating a yield curve that serves as benchmark for private sector financial intermediation.

The economic recovery of **Uruguay** continued in 2005, with GDP growth reaching 6.6%, in spite of the deterioration of its terms of trade generated by higher oil prices and the slight decline in the prices of some of its main exports. Output growth was driven by booms in manufacturing industry and services, where electricity, gas and water, commerce, restaurants and hotels stood out. In 2006 an economic expansion nearing 4.5% is expected, supported by the dynamism of said sectors as well as that of agriculture. Similarly, the consumer price index posted a variation of 4.8% in 2005, a rate within the range established by the government's monetary program (5-7%). Regarding employment, a slight improvement was registered, as unemployment fell from 13.1% in 2004 to 12.1% in 2005. The fiscal situation remained relatively favorable, with a consolidated deficit of 2.5% of GDP, in a context of increasing tax revenues and stability in central government expenses. Finally, the current account of the balance of payments accentuated its negative balance from a deficit of 0.8% of GDP in 2004 to 2.8% in 2005.

**Venezuela** closed 2005 with a GDP growth rate of 9.3%, as a result of higher public expenditures and private consumption growth. The short and medium term petroleum scenarios foresee the maintenance of relatively high oil prices. This implies that the economic situation of Venezuela should be relatively comfortable in the next years from the growth, fiscal, and external standpoints. In the external sector, oil exports rose to record levels due to the high prices and, although imports also increased, the current account ended the year with a surplus of US$ 24,436 million (17% of the GDP). Fiscal management was also influenced in an important way by the oil windfall and, in spite of higher oil and non-oil revenues, public expenditures showed an important expansion. Nevertheless, financing needs have been reduced, allowing for greater reductions in public debt levels. The persistence of inflation is expected for the 2005-2007 period in a range between 13% and 15%, as well as the continued appreciation of the real exchange rate.

Regarding the Caribbean nations partners to CAF, **Trinidad & Tobago** experienced a year of good economic results in 2005. In a positive external context, given high fuels prices, the economy registered an expansion of 7%. Growth was boosted by fuel exports and construction and manufacturing sectors. This accounted for the creation of 28,000 jobs during the year, which decreased the unemployment rate to 8%. In terms of prices, the country registered an inflation rate of 6.8% with food products exhibiting the greatest increase (close to 23%). Strong growth is expected to continue in 2006 (close to 9%), as well as the maintenance of a healthy fiscal balance and favorable results in the external sector.

In **Jamaica**, GDP grew 1.4% in 2005 and an expansion of 2.9% is expected in 2006. Additionally, important foreign direct investment flows are expected in mining and tourism. Inflation reached 15.9% in 2005 due to the effects of foreign exchange depreciation, the shortage of agricultural products (due to hurricane Ivan) and the recent rise of food product prices. After four years of slow growth, the **Dominican Republic** closed 2005 with a GDP expansion rate of 9.3%, mainly as a consequence of consumption and private investment growth, especially in the areas of tourism, telecommunications and commerce. In spite of high oil prices, inflation closed the year at 7.4%, a significantly lower figure than in 2004. It is expected that growth will slow to 4.5% in 2006, the drive of the tourism sector will continue and the discipline in macroeconomic management will be maintained.

## External sector

A favorable international setting contributed to an increase in Latin American exports and a substantial rebound in prices of products.

As a result of a favorable international environment, especially due to the expansion experienced by industrialized countries and some important emerging economies, such as China and India, there has been an increase in the demand of primary goods and upward price pressures. In this context, the balance of payments of most countries in the region has posted surpluses, even reaching historical records in some countries. External accounts have also been strengthened by the rise in remittances, which have become, in some cases, the main source of hard currency. In the following years a slight deterioration of the trade balance is expected, in line with the acceleration in the growth rate of imports and lower rate of export expansion as a result of a slowdown in global demand and a slight deterioration in terms of trade.

External capital inflows to the region, even when important differences exist among countries, have resulted in a significant accumulation of foreign reserves, boosting the external position of Latin American economies. In general, the strength of external accounts is one of the main factors that support the reduction of country risk levels and strengthens the macroeconomic foundations of the region. This means that Latin American countries are now in a better relative position that in the past to confront future external shocks.

## Public finances and indebtedness

Even though fiscal management in Latin American countries has improved substantially in recent years, evidenced by the reduction of fiscal deficits and public debt levels, the medium-term sustainability of public accounts remains a weak point in some countries.  On the positive side, governments have taken advantage of the favorable conditions prevalent in capital markets, characterized by ample liquidity and a compression of sovereign debt spreads, as well as oil surpluses, in some cases, to improve the management of its liabilities. This has been achieved by improving debt profiles, extending terms of repayment and improving financial conditions. Debt issuance in internal markets has also been registered, where governments have managed to establish a reference yield curve for private sector bond issues, substituting external for internal debt under favorable terms. Debt issuance in domestic currency has reduced foreign exchange risks and has permitted taking advantage of the recent appreciation of local currencies to change the currency composition of liabilities.

Similarly, an improvement in fiscal institutions has been observed, especially in terms of their capacity to collect greater fiscal revenues. In spite of a low tax base due to significant evasion, numerous

**With an average of 6.9%, most shareholder countries posted moderate inflation rates, thus achieving greater economic stability and improving living standards**

tax exonerations and an important informal sector, governments have managed to increase fiscal revenues by means of administrative measures and greater collection efforts.

Nevertheless, in terms of public expenditures, a series of budgetary inflexibilities remain (payrolls, pensions, pre-allocations, current transfers, among others) as well as social demands for greater public spending, which increase the treasury's financing needs. These demands are many times difficult to finance, and limit the adoption of more countercyclical fiscal policies during economic downturns. The fact that oil-producing countries are not significantly saving their widfall makes fiscal policies even more procyclical. Though countries have begun reverting the trend to decrease public investment levels (in social and productive infrastructure), the fact that these investments are being financed with temporary revenues, and that contingent liabilities are accumulating, introduces uncertainty as to the future sustainability of these investments.

Finally, even when fiscal accounts appear sustainable in the majority of the countries in the region, as primary public savings allow for the repayment of public debt service and the maintenance of a constant debt to GDP ratio, sustainability is very sensitive to changes in key variables such as interest rates and the prices of primary goods, among others. This makes countries particularly vulnerable to changes in the external environment.

## Monetary, foreign exchange and financial sectors

A favorable trend of decreasing inflationary levels took place in most Latin American countries in 2005. Inflation fell to 6.3% from 6.8% in 2004. In the Andean Community, inflation decreased with respect to the previous year, going from 9.4% in 2004 to 7.7% in 2005, in spite of a higher inflation rate posted in Venezuela. In fact, the remaining Andean countries exhibited inflation rates below 5%. Similarly to 2004, prudent monetary policy and an environment of relative fiscal discipline influenced these positive results. Besides, the adoption of inflation targeting schemes in several countries contributed to the stabilization of prices, generating an environment conducive to price stability.

Nominal exchange rate stability has continued in the majority of Latin American countries. Nevertheless, growing capital inflows have generated an excess of supply in the foreign exchange market, which has exerted downward pressure on real exchange rates. This process of real currency appreciation has been a source of concern given the loss of competitiveness. In this sense, some of the region's central banks have implemented currency exchange policies to counter this appreciation trend.

In the financial sector, ample liquidity in international markets continued being an important factor in the orientation of global capital flows toward the region, prompted by the search of greater returns. In this context, and given the sound external positions of Latin American countries, the accumulation of reserves as well as the economic stability turned the region into an attractive option for international investors. This was reflected in higher bond issues and lower interest rate differentials. Similarly, there were favorable conditions for debt issuance in domestic currency in various countries of the region and changes in debt composition, with the purpose of reducing exposition to financial mismatches.

## Competitiveness

The positive macroeconomic performance described above can mask the presence of structural problems such as distorted labor markets and inefficient state bureaucracies, which adversely affect the business environment and limit GDP growth. Nonetheless, the present moment is an excellent opportunity to carry out an agenda of pending reforms in matters of competitiveness improvement. This becomes particularly necessary in light of the fact that productivity has decreased in most countries during

the last four years. According to the most recent Global Competitiveness Report published by the World Economic Forum, the majority of Latin American countries have worsened their relative position in the international competitiveness growth ranking.

This situation is also reflected in indicators that determine the quality of the business environment. Particularly, the difficulty to start or close a business impacts on overall productivity and on investment decisions. In this sense, the region is characterized for having difficult procedures that make the creation of new businesses very costly. In general, tackling investment climate and competitiveness problems become imperious needs when countries are trying to expand their participation in global trade through bilateral trade agreements. Hence, advancing the so-called internal agenda to improve productivity and competitiveness is a priority for most countries in the region.

**Latin American countries are giving priority to social issues in their public policy agendas and taking actions to improve the quality of social investments**

## Poverty and social indicators

Even when the macroeconomic and growth outlook is favorable for Latin America, a less promising story of high poverty and social exclusion persists in the region. Nevertheless, as a consequence of economic growth observed during the last three years, per capita income levels have improved, and poverty and unemployment have slightly decreased. Also, real salaries have increased in some countries and, in general, human development indexes, according to UNCTAD, have shown advances in the entire region. In spite of these advances, it is a fact that further improving the welfare of the majority of the population in Latin America is still pending.

The region continues being the most unequal one in the world in terms of income distribution, with an increasing gap within countries (between rural and urban areas, and within urban areas) and growing exclusion and economic and social marginalization. Even more, the fact that the majority of countries are deepening their participation into the global economy increases their vulnerability to external shocks, with the poorest segments of society usually being the most vulnerable. Additionally, even if there have been significant advances in some countries toward the fulfilment of the Millennium Development Goals such as the provision of basic services, education and health, it is unlikely that poverty and social exclusion reduction goals will be met by 2015.

Improving social conditions has turned into one of the main priorities in the public policy agenda of Latin American countries. This has been embarked in multiple ways, including the attainment of strong economic growth as a necessary condition to generate employment. In the same way, in addition to assigning an important share of the national budget to social sectors, countries are set to improve the quality and management of social investments, which in many cases are considered inefficient. This is reflected by the fact that higher social spending has not necessarily translated into improvements in social indicators.

The public policy agenda should also be more focused on the creation of opportunities, rather than in aid policies. This includes the provision of micro-finance, social investment funds with adequate incentives, social responsibility programs, formalization of assets, among others. The maintenance of social safety nets for the most vulnerable segments of population to external shocks and natural disasters should also be given special importance. In this context, it is necessary to have a countercyclical social fiscal policy. Finally, as a long-term task the accumulation of human capital must be privileged, in terms of improvements in education and health services.

## Institutions and governance

The positive results previously described, characterized by strong economic growth and moderate improvements in some poverty and inequality indicators have been achieved in a context of political and institutional difficulties in some countries. This has led some analysts to describe the existence of a "divorce" between political and economic variables. In 2005 serious institutional weaknesses were made evident at the outset of governance crises in some countries. Similarly social pressures increased with public demonstrations in several countries, evidencing disenchantment with serious disparities that still persist in the region.

Moreover, in spite of the large approval ratings of some of the region's leaders, there is popular discontent with the functioning of democracy. This is corroborated by Latinobarometro's latest survey, according to which only half of Latin Americans firmly believe in democracy and only one in every three citizens is satisfied with its functioning (these results have remained similar during the past three years). Similarly, only a fifth of those polled acknowledge having confidence in political parties, and 25% in Congress and the justice system.

During 2006, the political agenda in Latin America will be very active with presidential and legislature elections in thirteen countries. This presents a challenge for Latin American politicians in a context of popular dissatisfaction with the current political system. Nevertheless, this situation also presents a great opportunity for leaders to take advantage of their high approval ratings to carry out necessary political and institutional reforms and to promote needed consensus building.

## Regional integration and participation in global trade

**CAF promotes deeper integration in Latin America to achieve the countries' union through strategic programs and physical integration projects, as well as sustainable, equitable and inclusive development**

In spite of the deceleration of world trade in 2005 –resulting in part from the strong rise in oil prices–, regional trade, and particularly intraregional trade, has continued recovering from the crisis that affected Latin America between 1999 and 2003. This is evidenced by the fact that the rate of growth of intraregional trade surpassed the one registered with the rest of the world.

At present, the countries of the region are immersed in multiple spheres of international trade negotiations. These spheres are articulated around three main axes: regional integration agreements, trade agreements between developed and developing countries outside the region, and multilateral negotiations within the framework of the World Trade Organization (WTO). Particularly, several Latin American countries are negotiating a Free Trade Agreement (FTA) with the US as an essential part of their international trade strategy. It is important to underline that these diverse options are not mutually exclusive and are part of a coherent strategy of participation in global markets.

The nations of Latin America recognize the importance of the multilateral route for an effective participation in international markets, and are therefore actively involved in the negotiations of the Doha round. The year-end meeting in Hong Kong gave momentum to the negotiations, after they had languished considering the failure of previous meetings in Cancun and Seattle. For Latin American countries, the most important achievement was the commitment by industrialized countries to eliminate subsidies to agricultural goods exports by 2013. With this, 60% progress has been attained. Nevertheless, worries remain about concluding an agreement before the end of 2006, given that *Trade Promotion Authority* in the US will expire in July 2007.

Progress in matters of integration and regional trade agreements took place in 2005, especially related to the establishment of the South American Community of Nations. Additionally, the CAN-MERCOSUR and Peru-MERCOSUR free trade agreements took effect, liberalizing 80% of trade between the two blocks. The remaining 20% of trade, which includes sensitive products such as agricultural goods, will be liberalized during the next 14 years. In addition, an agreement was signed by which Venezuela will enter MERCOSUR as a full member, once a series of commercial and political requirements are met, and the agreement is ratified by the Congresses of the five participating countries.

Regarding hemispherical integration, the initiative to constitute a Free Trade Area of the Americas (FTAA) has lost importance. The Summit of the Americas held in Mar del Plata, Argentina, evidenced strong differences of positions in the region: on the one hand, the US, Mexico, Central America and other South American countries agreed to advance in the negotiations and, on the other, MERCOSUR country members and Venezuela decided to postpone these negotiations waiting for the outcome of the Doha Round.

In view of this, the US and several countries in the region have decided to pursue bilateral negotiations. In this context, the American Congress ratified, by a very small margin, a free trade agreement (FTA) with Central American countries and the Dominican Republic (CAFTA-RD). Peru has recently ended negotiations of a FTA with the US, while Colombia and Ecuador expect to end these negotiations at the start of 2006. The FTA between Panama and US should also be concluded in 2006 despite the difficulties that have been found in the negotiations related to agriculture.

Finally, it is important to highlight the negotiations with countries outside the region. In that sense, the trade agreement between Mexico and Japan, which was signed in 2004 and took effect this year, stands out. This agreement implies that Japan will gradually eliminate 91% of the applicable tariffs to Mexican products, until their complete elimination in 2014. On the other hand, the trade agreement between Chile and China signed this year is the first of its kind between the latter and a Latin-American country. Also, the Trans-Pacific Strategic Economic Association Agreement was subscribed between Chile, Brunei, New Zealand and Singapore. The negotiations for a Panama-Singapore agreement were also concluded and negotiations between Singapore and Mexico and Peru have began.

## Presence of CAF

Official photograph of the Mercosur Summit (Montevideo, 8 to 9 December 2005), in which CAF was recognized for its contributions to the physical integration process in South America and its role in promoting coordination between Mercosur and the Andean Community.

As a fundamental pillar of its mission, CAF has kept its commitment to regional integration through the years. Today, when the number of shareholder countries reaches 17, including practically all of South America, as well as various countries from Central America and the Caribbean, and Mexico and Spain, CAF is advancing toward a deeper integration viewed in an integral way. Although this focus has emphasized the promotion, structuring and financing of physical infrastructure projects, it also includes other objectives like the promotion of macroeconomic convergence, competitiveness, capital market development, social, cultural, political, and commercial integration, governance and corporate government, among others. All these elements contribute to the objective of promoting the sustainable development of CAF shareholder countries.

In this context, during 2005 CAF has consolidated its support to the strengthening of the hemispheric and Latin American and Caribbean integration processes. The presence of its executive president, Enrique García, in the main regional forums held this year, enabled CAF to actively participate in the regional dialogue on the fundamental issues confronting each one of the different integration schemes.

Committed to the goal of regional convergence, in the framework of the Summit of the Americas celebrated in Mar del Plata (Argentina), the Andean Summit in Lima (Peru), the presidential meetings of MERCOSUR in Asuncion (Paraguay) and Montevideo (Uruguay), the Foreign Affairs Minister Meeting and the First Summit of Heads of State of the South American Community of Nations in Brasilia (Brazil), the Summit of the Association of Caribbean States in Panama, as well as the meetings of the Puebla-Panama Plan, CAF presented its vision and commitment with a strategic integration agenda, in order to promote the goals of physical and energy market integration, trade integration, social development and environmental goals.

In the achievement of this vision, CAF has strengthened institutional synergies, through the implementation of work programs and cooperation projects, with different agencies and regional inte-

## New CAF contribution to regional development

The second edition of the Report of Economy and Development (RED), titled “Latin America in global trade: advancing market access” was published by CAF in 2005.


Written by research professionals at the Corporation, with participation of renowned regional scholars, this document aims to contribute to the debate on how to achieve quality and sustained economic growth in Latin America that translates into benefits for all its citizens. In this sense, expanding the participation of the region in global markets no doubt constitutes a key component of a development agenda that seeks to achieve high economic growth that is sustainable and inclusive.

Although Latin America’s international trade has grown in a significant and accelerated manner since the reforms undertaken during the last two decades, the region’s participation in world trade has diminished and represents less than half of its participation forty years ago. This reality has mainly been a consequence of, on one hand, the persistence of important trade barriers, and on the other, the existence of a logistic platform, especially regarding ports and customs, which add costs and creates additional obstacles to trade.

The region needs to build a coherent strategy of negotiation given the multiple trade options available. For each country there will be a specific correspondence between the need for greater trade liberalization and the particular options at its disposal. Deepening Latin America’s participation in international trade calls for a strategy established according to country-specific factors, relative comparative advantages and particular national interests.

Moreover, the selection of an adequate trading route (or group of routes) requires a good understanding of the costs and benefits associated with the different alternatives available to countries. This implies the need to determine and evaluate the aggregate, sectoral and social impacts of all negotiation spheres. The evaluation of social impacts is especially important reflecting the growing interest among policy makers in determining the political feasibility of these agreements, which largely depends on the impact of trade liberalization on key variables such as employment creation, income distribution and poverty reduction.

In general, the evidence presented in the report is clear in showing that, even taking into account different agreement’s characteristics, trade liberalization has positive economic and social impacts for its signatories.

On the other hand, even though there is consensus that non-discriminatory trade liberalization within the World Trade Organization (WTO) framework would generate greater benefits than preferential trade agreements, its relative slow pace and the complexity of its negotiations has given way to the pursuit of alternative agreements, especially bilateral ones. Furthermore, aggressive bilateral compromises could help sub-regional blocks advance their internal process of political integration and harmonization.

The strengthening of regional agreements may also provide more leverage to smaller economies when facing more stringent multilateral obligations.

Notwithstanding, it is also important for Latin American countries to pursue trade liberalization in the multilateral context. Clear and definitive advances in agricultural liberalization, for instance, can only be achieved within the WTO, insofar as it comprises all member countries.

Naturally, trade liberalization cannot be the only foundation on which a global integration project should be based.

Further trade liberalization should be accompanied by complementary policies in other areas, such as improvements in air and maritime customs and technical norms, as well as increased coordination and policy harmonization, among others.

In this sense, advances in trade facilitation will increase effective access to world markets. All of this must be complemented with more investment in infrastructure.

The benefits of doing so will boost export potential and improve overall competitiveness.

In this context, CAF hopes to contribute with this book to stimulate debate and guide the public policy making to further access international markets with the ultimate goal of achieving more growth and better quality of life for the region’s inhabitants.

gration secretariats, including the OAS, the General Secretariat of the Andean Community, the Permanent Representatives Committee of MERCOSUR, the ALADI, the Organization of Amazon Cooperation Treaty and the Association of Caribbean States. Similarly, as an essential part of its commitment with integration, CAF gave special importance to programs and projects of border development and integration in shareholder countries.

Moreover, CAF has actively participated in the academic debate on how to attain high quality growth with equity. The 2005 edition of the Report of Economy and Development, titled "Latin America in global trade: advancing market access" focused on how to deepen the participation of Latin American economies in international trade ( *previous page*).

CAF's Executive President informs Brazil's President Luiz Inácio Lula da Silva about the progress of the programs financed by CAF in South America.

CAF's Executive President next to the participants of the first Meeting of Foreign Ministers of the South America Community of Nations (Brasilia, 19/APR/05) where CAF highlighted the role that it plays in financing integration infrastructure projects, especially in the framework of the IIRSA Initiative. The meeting manifested the will of South American countries towards developing an integrated space in political, environmental, economic and infrastructure terms.

# 35

# 35 years of commitment to sustainable development and regional integration

**Over the past decade, CAF has earmarked nearly US$ 62,000 million to finance projects for development in its shareholder countries**

**CAF has not only survived hard times in Latin America but posted steady growth to become a renowned and solvent financial institution**

ON 8 JUNE 2005, THE ANDEAN DEVELOPMENT CORPORATION celebrated its 35th Anniversary, with accumulated approvals amounting to over US$ 43,000 million, disbursements exceeding US$ 30,000 million, and a total loan and investment portfolio of over US$ 8,000 million at the end of 2005.

In its 35 years of existence, CAF grew progressively from a small subregional financial institution to the main source of multilateral financing to the Andean Community countries. It also became an important financial alternative for the other shareholder countries, thanks to its anti-cyclical and catalytic role, which allows it to meet its clients' requirements flexibly and dynamically, especially in difficult times.

CAF's catalytic action has mobilized resources of nearly US$ 62,000 million over the past decade for sustainable development and regional integration projects in shareholder countries. This amount includes financing by CAF and its clients, as well as other local and non-regional sources.

As it became the most successful regional bond issuer during the 1990s, CAF helped Latin American countries regain access to international financial markets, after the recurrent economic crises that affected the region, mainly as a result of a complex global environment.

In compliance with one of its basic institutional objectives –promoting regional integration– CAF has contributed to having Latin America taken more into account at various international decision-making processes. During the past few years, the Corporation also strengthened its role as intercommunicator among various regional integration schemes, particularly the Andean Community and Mercosur in South America.

CAF has also been recognized for its strategic regional programs aimed at promoting competitiveness, integration, governance, and the development of cultural, human, social and environmental capital; those programs also foster the development of micro-, small- and mid-sized enterprises and promote a more effective and equitable international insertion.

CAF also plays a fundamental role in modernizing the region's infrastructure for physical integration –especially in South America– based on principles of environmental and social sustainability, attainment of economies of scale, and the use of innovative financial investment mechanisms, with a view to strengthening the regional integration processes.

On another strategic line of action, CAF is promoting the adoption of a renewed development agenda for the region, which focuses comprehensively on combining macroeconomic stability and microeconomic efficiency with social solidarity, to achieve sustained and equitable growth. This conceptual agenda is the result of the need to address critical and recurrent problems affecting the region, including macroeconomic imbalances, insufficient and unsustainable growth, social tensions stemming from poverty, unemployment and social exclusion, border conflicts, volatile international capital flows, vulnerability to external shocks, strong dependence on raw material exports, and low levels of competitiveness.

## Changes in the regional and global environment

At the time CAF was created, most of Latin America followed an inward-looking development approach, characterized by rather closed and centralized economies. CAF's first managers faced the complex task of kick-starting the Corporation's activities, obtaining the initial financial resources, defining operational criteria, organizing the staff and the administrative department, gaining the confidence of banks and international financial institutions, and ensuring an adequate response from clients and investors, among others.

Undoubtedly, management of the early years made valuable contributions which would establish the basis to transform CAF from a traditional development promotion organization –which operated

**Over 35 years of existence, CAF has enjoyed strong support from shareholder countries, which have increased their equity participation on a regular basis and timely paid their quotas**

only with the resources provided by its member states– into the highly competitive financial institution which it has become, both in a regional and global context, even though those contexts were not always favorable. For example, the two integration areas in which practically all of CAF's projects were concentrated during the seventies as a result of the Corporation's operational policies, the region's industrial programs and trade liberalization processes, practically came to a halt in the late 70's.

Later, at the beginning of the so-called "lost decade" of the 1980s, both the Andean region and the rest of Latin America were severely affected by a profound economic crisis resulting from its external debt burden, the fall in its export prices and an overall decrease in global trade. This led CAF to increase its areas of activities by adopting new operational policies which allowed the Corporation to operate on a more independent basis.

Given the financial environment, at the time it was almost impossible for CAF to work with international private banking institutions, as a result of which the Corporation had to change its financial strategy.

The entire Andean Group was affected by this prolonged economic stagnation and the regional integration process suffered major setbacks. Nevertheless, the complex situation which prevailed led to significant changes in the orientation of the Andean Group, which received strong and unanimous support from Andean Presidents. At regular summit meetings, the Andean Presidents supported the Corporation and the integration process, by increasing its scope and resources, such as the decisions to double its authorized capital (Galapagos Summit, December 1989) and to invite other Latin American countries to participate as shareholders (Caracas Act, May 1991).

## New trends in the development process

In the early 1990s, the countries of the region undertook important structural changes in their development plans; those included greater commitment to openness of their economies and to greater foreign competition as well as a more active participation by the private sector, while strengthening democratic institutions and governance. The international situation contributed to the adoption of this new approach. Indeed, the events in Eastern Europe and the Soviet Union –which eventually led to the fall of the Berlin Wall in 1989– seriously challenged the centralized economic development model, in which the public sector dominated the productive and financial sectors.

The agendas of the governments throughout the region began to include issues related to macroeconomic stability, efficiency, equity, sustainability, democracy and integration. There was significant progress in key areas such as the fiscal and monetary sectors, market competitiveness, trade opening and institutional reform, among others. Nevertheless, the challenges facing the region continued to be very significant, given an international context of globalization and competitiveness, which required an equitable insertion into global markets.

In response to these new factors which conditioned the region's development, CAF outlined and put into practice a new operational and financial strategy for the medium and long terms; these strategies were the result of consultations with the governments of shareholder countries, the members of the Board of Directors, multilateral and bilateral financial organizations, investors and other personalities from within and outside the region, as well as representatives of the environmental, social and economic sectors. At the same time, CAF undertook a thorough institutional restructuring –which covered policies, procedures, systems and organization– with a view to optimizing processes and achieving the highest possible level of competitiveness in order to meet the requirements of its clients, and those of its external financial sources and the credit rating agencies. The results of this restructuring are evidenced by the impressive results obtained by CAF during the financial crises that affected most of the countries in the region, as well as the outstanding results attained during periods of greater stability and prosperity (*pp. 28 and 29*).

## Shareholder countries' actions to strengthen CAF

**1970** CAF started operations on 8 June, with an authorized capital of US$ 100 million.
**1974** CAF held its first Shareholder's Extraordinary Assembly, in which Member States expressed their solidarity and willingness to strengthen CAF in operational and financial terms, by raising its authorized capital to US$ 400 million.
**1985** In spite of the serious economic crisis that Andean countries faced this year –as it was almost impossible for them to have access to private capitals– they gave priority to CAF's capitalization need, by increasing its authorized capital to US$ 1,000 million.
**1989** The private sector started to participate in CAF's paid-in capital, by increasing to US$ 50,000 million the capital accounted by *Series B* shares, in order to be undersigned by commercial banks and private financial institutions of Andean countries, with the incorporation of one private sector representative into the Board of Directors.
**1990** As a demonstration of the Andean Presidents' strong support to CAF, in July 1990 the Corporation's authorized capital was duplicated from US$ 1,000 million to US$ 2,050 million.
**1996 / 1998** Further increases in CAF's authorized capital to US$ 2,500 million and US$ 3,000 million, respectively, were approved along with a series of amendments to CAF's Constitutive Agreement related to governance and strengthening of the institution's financial policies. Furthermore, in 1996, *Series C* shareholders (non-Andean countries) were granted representation in CAF's Board of Directors.
**2002** In a new demonstration of their consistent support, shareholder countries increased CAF's authorized capital from US$ 3,000 million to US$ 5,000 million. Additionally, it was approved to increase the presence of *Series C* shareholders in the Board of Directors with two Directors and twoAlternates.
**2005** In October , it was subscribed the Protocol to Modify CAF's Constitutive Agreement, a historic reform unanimously approved at Shareholder's Extraordinary Assembly which, upon ratification of the five Andean countries Congresses, will allow the 12 *Series C* shareholder countries in Latin America and the Caribbean (as well as other countries in the region) to have access to full membership as *Series A* shareholders.

### Efficient and timely response

Since its creation, CAF has maintained continuous presence in its member countries, by tailoring its activities to meet their requirements and priorities. In the context of the process of institutional strengthening and modernization, CAF clearly outlined its mission on the basis of two fundamental pillars –sustainable development and regional integration– as well as its support to the efforts of its shareholder countries to further diversify their economies, make them more competitive and responsive to social needs, and provide strong support to the private sector.

As its mission was widely supported by its shareholders, CAF continued to undertake actions that boosted the countries' agendas for change, strengthened the sectoral approach and provided a timely response through structured mechanisms with a catalytic effect.

In 2000, CAF created the Vice-Presidency of Country Programs to deepen the strategic alignment with its partners' goals. At the beginning of each presidential term, CAF conducts programming missions. With the participation of a multidisciplinary technical team headed by the executive president, these missions establish an agenda for dialogue to bring its institutional capacity for technical and financial support into line with national priorities. Afterwards, it establishes a formal mid-term working commitment by issuing a joint statement endorsed by the presidents, which is updated on a regular basis.

### New partners, new business opportunities

Another relevant accomplishment made during the 1990s was CAF's decision to open its capital for participation of other partners in Latin America and the Caribbean –which demonstrates CAF's readiness to support integration. This allowed the Corporation to expand its operational base by creating new business opportunities with increasingly higher degrees of profitability and efficiency, while decreasing risks by diversifying its investment portfolio and becoming a leading institu-

## Thirty-five years in figures

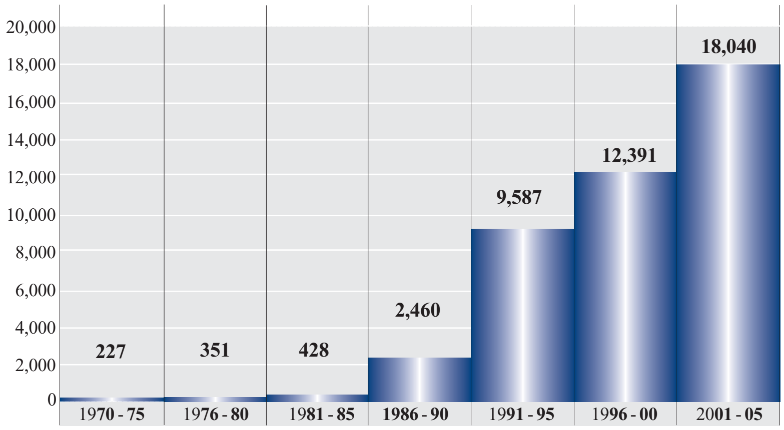
CAF's outstanding results throughout its 35 years of existence are reflected in its indicators on capital, portfolio quality, administrative efficiency, and profitability, as shown in the tables.

Over its last five-year periods, CAF has experienced an extraordinary growth –at both internal and external levels– adapting itself to these new dimensions in order to respond to changing global dynamics in a rapid and competitive way, and to satisfy the needs of its clients on a timely basis.

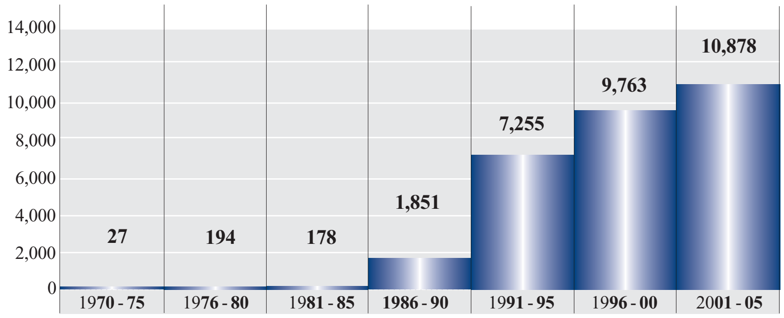
Since 1994, CAF uses a portfolio review system to monitor overall quality of risk financial assets (loans, investments, guarantees and stock participations). It includes permanent internal reviews and a periodical review conducted by external consultants, who abide by internationally accepted bank regulations.

At end of 2005, CAF's approvals totaled US$ 43,479 million, equitably distributed among shareholder countries.

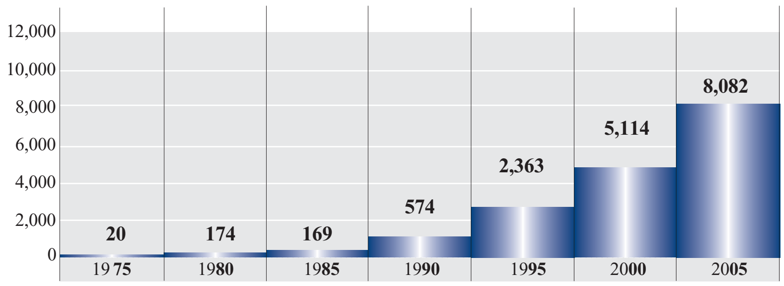
**Total approvals** US$ millions




**Total disbursements** US$ millions

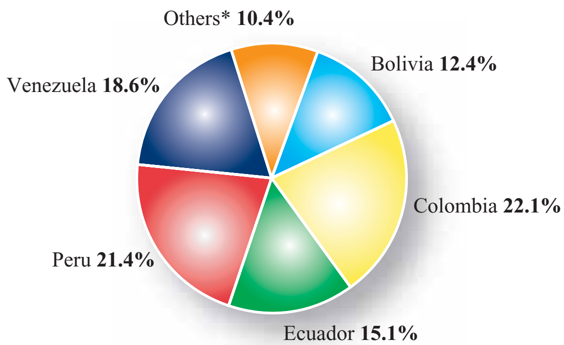



**Total portfolio*** US$ millions




* Includes the cofinanced component of CAF's portfolio and loans supported by CAF's partial credit guarantee program.

**Approvals by country (1970-2005)** US$ millions




* Includes *Series C* shareholder countries and multinational operations.

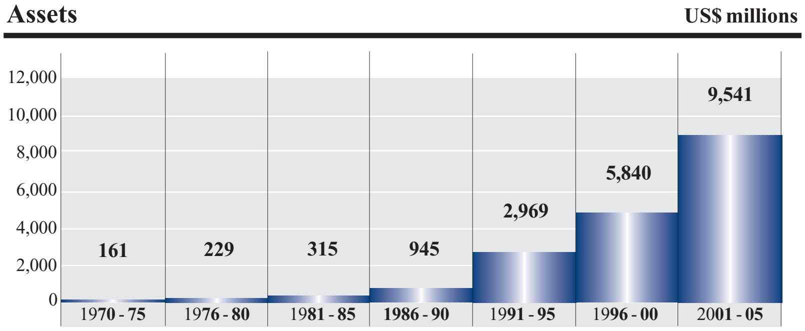
## Thirty-five years in figures

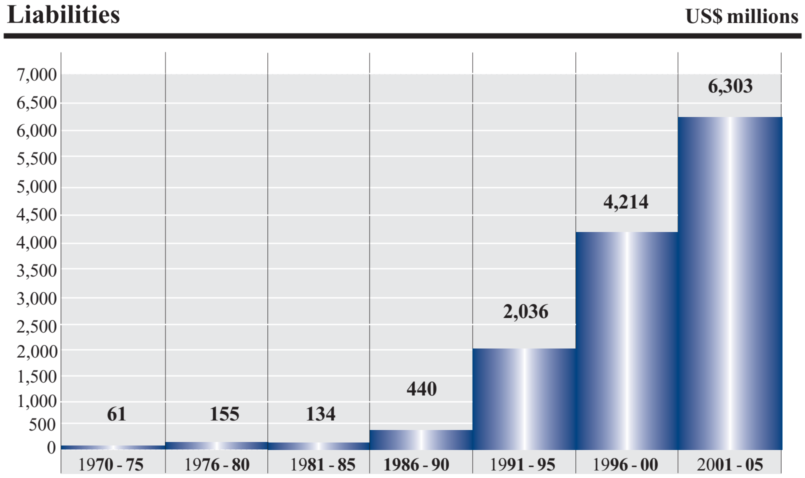
As the number of CAF's activities consistently increase, its total assets continue to grow at an average annual rate of more than 18% over the last 15 years.

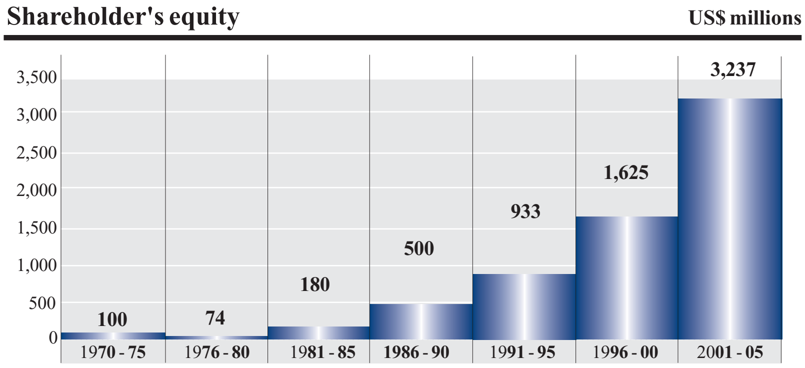
CAF's administration intends to use resources from third parties more efficiently, reducing their proportion with respect to the capital provided by shareholders.

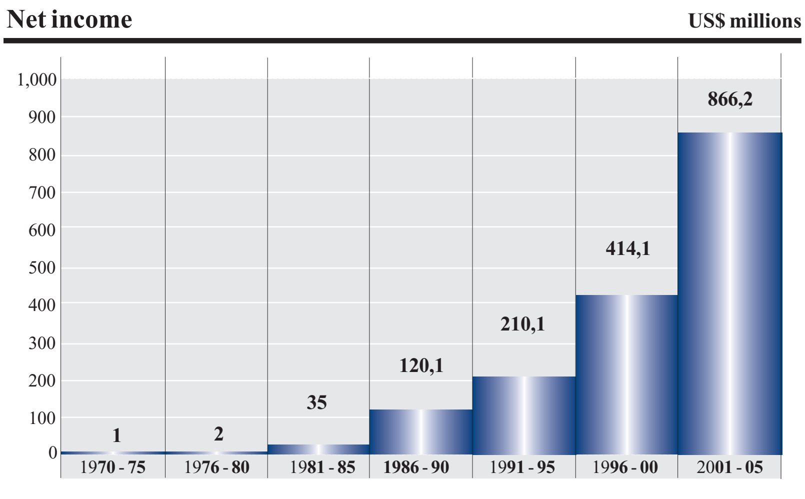
The capitalization indicator stands above the minimum 30% established in CAF's internal policies, substantially higher than the minimum 8% required for banks in general, according to the standards and regulations of the Basel Committee on Banking Supervision.

Sustained profit increases have allowed CAF to boost its equity capital, while maintaining consistent growth in its loan portfolio.

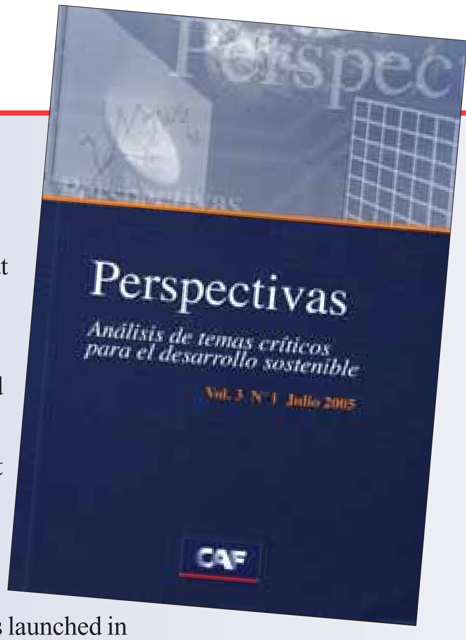


## Agenda for research on development issues




Knowledge has become an indispensable element in the current productive processes and, in view of its strategic importance, it is a major issue for Latin America.

Several years ago, when the challenges posed by the changes at the global level became apparent –and with the emergence of the knowledge and information society and the new conditionalities associated with economic performance– CAF started to outline its own Agenda for research on development issues and a strategic Action Plan in critical areas, within the framework of regional identity and cooperation and an integral vision of the adaptation process that was drawing near, in order to efficiently meet the requirements of shareholder countries. Thus, at the external level, the Corporation began to work with renowned personalities and experts from inside and outside the region on a broad agenda of issues for debate, and to reinforce its presence at the various forums looking for concrete responses as regards the issue of sustainable development.

With the support and synergies provided by its own professionals, the Corporation started to generate an amount of critical and innovative thought, which makes use of, and disseminates information about, the knowledge database that the region has built from the forums, publications and special programs carried out by CAF. As a matter of fact, in 1996, CAF created the Direction for Economic Studies. Its main objectives are:

to conduct in-depth analyses of the most important macroeconomic issues for Latin America; to provide technical inputs for various business areas, which can serve as guidelines for decision-making; and to undertake specific research projects.

Later on, with the creation of the Vice-presidency for Development Strategies in 2000, the knowledge generation process was further reinforced.

In 2003, CAF launched its first program to support research on development issues, with the purpose of generating, promoting and disseminating its own knowledge about regional development and integration, while actively supporting the design and implementation of economic and integration policies in the region. To this end, resources from technical cooperation funds were earmarked through an international facility for financing research projects on relevant issues for the region. This initiative gave priority to financing Latin American researchers at renowned universities. In addition, the Corporation opened up the possibility to admit guest researchers at its headquarters.

From its very beginnings, this program was widely accepted by the international academic community, particularly in the region, and has served as a basis to generate knowledge that has been disseminated through various seminars and publications. It should be mentioned that the research works carried out under the program have been published in the six-monthly bulletin "Perspectivas", which was launched in 2003. In addition, the conclusions of the studies carried out under the program to support research are included in the Corporation's flagship annual publication Report on Economy and Development, which analyzes issues such as insertion of the region into the global economy, productive transformation of the economies, and the challenge posed by social insertion.

Similarly, with the assistance of renowned international academicians and professionals working in the Corporation, CAF has undertaken specific research projects that have generated knowledge in the areas of fiscal sustainability, sectoral policies to support the productive sector, and competitiveness. The results of these studies have been disseminated through various events and publications.

The results of the researches sponsored by CAF are the subject of top-level debates with the officials responsible for economic policy in the region, and constitute a fundamental tool to maintain a constructive dialogue on development-related issues with the shareholder countries of the institution.

Furthermore, CAF's Direction for Sectoral Programming and Analysis issues regular reports on the Corporation's activities in the areas of electricity, transportation and telecommunications in South American countries. The reports are aimed at: 1) disseminating knowledge and best practices in the countries as regards regulations, norms, legal provisions and market participation; 2) making public policy proposals to enhance coverage, efficiency, effectiveness and sustainability in each sector; 3) attracting investment by disseminating information about the major projects and needs in the various industrial sectors; 4) analyzing the evolution of these sectors so as to understand the difficulties they have faced in undertaking changes; and 5) offering support to the private and public sectors and to government institutions in order to promote such changes.

tion supporting integration. Since the entry of the first non-Andean country (Mexico, in 1990) to date, the number of shareholder countries and *Series C* countries has increased to 12, including Spain.

The participation of these new actors and consequently, the additional opportunities for integration, as well as the new outlook for modern and efficient financial operations, has been a crucial factor in strengthening the unity and competitiveness of Latin America and the growth of CAF. This is clearly evidenced by CAF's action since 1992 based on the concept of competitive logistics. In the area of sustainable integration infrastructure, CAF has provided support to railroads, river and road corridors, air and maritime transportation, gas pipelines, electrical and telecommunication networks, in addition to its dynamic participation in the IIRSA Initiative.

The entry of Spain in 2002 –the only non-Latin American partner– has strengthened CAF as a financial institution and has allowed Latin America to tighten its traditional economic, cultural and political ties with that country and, through it, with the European Union.

### Date of income
*Series C* shareholders

| | |
|---|---|
| Mexico | 12/OCT/1990 |
| Chile | 18/AGO/1992 |
| Trinidad & Tobago | 24/JUN/1994 |
| Brazil | 30/NOV/1995 |
| Paraguay | 18/FEB/1997 |
| Panama | 17/NOV/1997 |
| Jamaica | 01/DIC/1999 |
| Argentina | 29/AGO/2001 |
| Uruguay | 11/DIC/2001 |
| Spain | 18/FEB/2002 |
| Costa Rica | 04/MAR/2002 |
| Dominican Republic | 29/DIC/2004 |

### CAF's shareholder countries

**1970-1989**

- Bolivia
- Colombia
- Ecuador
- Peru
- Venezuela

**2005**

- Bolivia
- Colombia
- Ecuador
- Peru
- Venezuela
- Argentina
- Brazil
- Costa Rica
- Chile
- Dominican Republic
- Jamaica
- Mexico
- Panama
- Paraguay
- Spain
- Trinidad & Tobago
- Uruguay

With approvals surpassing US$ 3,500 million, disbursements over US$ 2,000 million, and a US$ 787 million investment portfolio, CAF has become increasingly important for non-Andean countries, thanks to its ability to consistently update its programs and identify priorities with governments in order to outline joint strategic actions.

## Infrastructure for integration, competitiveness and social inclusion

During its first two decades of existence, CAF gave priority to financing its member states in international trade, and to this end, a high percentage of its investment portfolio consisted of short-term credit lines for the private banking sector aimed at promoting exports. Infrastructure accounted for a marginal percentage and financing only to supported equipment imports and not infrastructure projects.

## Roads for integration:

### Outstanding CAF infrastructure projects

**Ecuador: Amazonian link to Colombia and Peru (Carretera Troncal del Oriente).** Low-altitude road corridor that goes along the eastern mountainside of the Andes, which allows for vehicular traffic among Venezuela, Colombia, Ecuador and Peru, thus facilitating the development of new productive and social activities in relatively isolated or marginalized areas. *CAF's contribution: US$ 93,8 million* of a total US$ 152,7 million investment made thus far.

**Brazil: Road and electrical supply interconnections between Brazil and Venezuela.** This project included resurfacing work and improvements of road BR 174 stretching from Manaos to the border with Venezuela. Thus, a communicating road was opened between the state of Roraima and the Caribbean through Venezuela and Colombia. The project was complemented with the electricity transmission system between Santa Elena de Uairén (on the Venezuelan border) and Boa Vista (Roraima state). *CAF's contribution: US$ 172 million* of a total US$ 379 million investment.

**Peru: Northern Amazonas Road Corridor.** It connects the ports of Paita, on the Pacific coast, and Yurimaguas, on the river Huallaga. The project will facilitate the integration of three regions in Peru, benefiting a population of eight million inhabitants. In addition, this corridor will serve to connect the Pacific and Atlantic coasts in South America, consolidating the 5,000 km-long Interoceanic Multimodal Corridor, between the port of Paita in northern Peru and the delta of the Amazon river in Brazil. *CAF's contribution: US$ 110 million* of a total US$ 328 million investment necessary for the project.

**Peru: Southern Interoceanic Road Corridor, sections 2, 3 and 4.** With a total length of approximately 2,600 km, this road between Peru and Brazil will benefit the Peruvian departments of Cusco, Puno, Moquegua, Apurímac, Arequipa and Tacna, towards the Atlantic coast and through the Madeira-Amazon waterway. *CAF's contribution: US$ 210 million* of a total US$ 1,073 million investment foreseen, which will be allocated through an innovative public-private financing mechanism.

**Bolivia: Integration Road Corridor Santa Cruz-Puerto Suárez, sections 3, 4 and 5.** This 600 km-long corridor is one of the biggest missing stretches for physical integration in South America. The road between Santa Cruz de la Sierra (in Bolivia) and Corumbá (in Brazil) is the best option for a direct connection with the greatest potential for economic and social development, aimed at establishing trade exchanges by land between the two countries and between the Andean Community and Mercosur. The projects will facilitate access to Puerto Bush, located 9 kilometers away from the Puerto Suárez fluvial terminal, which allows Bolivia to have direct transportation through the Paraguay-Paraná waterway as well as access to the Pacific Ocean. *CAF's contribution: US$ 280 million* of a total US$ 600 million investment necessary for the project.

**Bolivia: Bolivia-Argentina Integration Corridor.** The precarious conditions of roads have hampered the development of substantial trade flows between the southern region of the Bolivian Altiplano and the provinces in north-western Argentina. For this reason, since 2001, CAF has financed important projects to construct a north-south road corridor of crucial relevance for the integration of these regions, such as the Tarija-Bermejo, Tarija-Potosí and Potosí-Tupiza-Villazón roads. *CAF's accumulated contributions: US$ 194 million* and US$ 492 million of investment.

**Bolivia-Brazil: Gas Pipeline.** This project included the construction and operation of a gas pipeline between the two countries to export Bolivian gas to specific delivery sites in Sao Paulo and other Brazilian cities. With a length of about 3,061 kilometers –of which 563 kilometers were constructed in Bolivia– this gas pipeline has been operating since 1997 with a highly positive and strong impact on Bolivia's economy and trade balance, as it has opened a new export market. *CAF's contribution: US$ 215 million* of a total US$ 2,055 million investment required for the project.

**Uruguay: Megaconcession for the construction of major roads connecting Argentina and Brazil.** The Government of Uruguay granted concessions for maintenance and improvement of 1,272 km of National Primary Network roads and 2.904 m of structures (bridges and grade crossings, among others). This project will contribute to consolidate corridors for Mercosur's cargo imports and exports. The works included in the megaconcession required annual investments of approximately US$ 40 million during the first three and a half years. *CAF's contribution: US$ 25 million.*

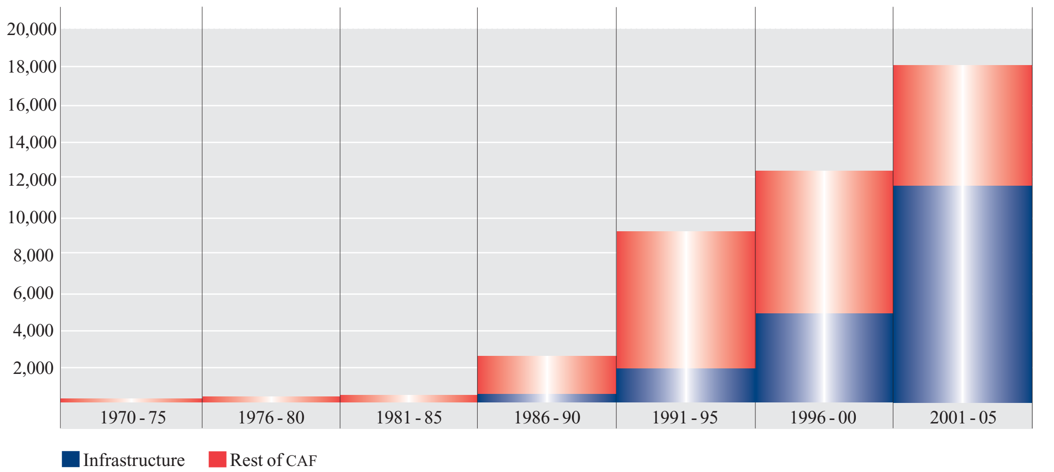
**Argentina: Surfacing work of Road RN 81 and access to Paso de Jama (Argentina-Chile).** These projects form part of the central corridor Capricorn Hub within the context of the IIRSA Initiative and serve to integrate the northern regions of Chile and Argentina with Paraguay and Brazil. The trans-Andean Paso del Jama border crossing offers favorable conditions for cargo truck traffic among the countries of Mercosur, Bolivia and Chile, and from these countries to other markets in the main urban and industrial areas of the rest of the region. *CAF's contribution: US$ 70,6 million.*

Noteworthy, the first of the very few loans approved for the infrastructure sector was for an integration infrastructure project in 1972. The US$ 3 million loan improved road connections between Venezuela and Colombia with the construction of a bridge over the river Limón in Zulia State, Venezuela.

Twenty years later, CAF's administration initiated its rapid growth supporting the infrastructure sector, by implementing an ambitious physical and border integration plan in 1992. Fully aware of the isolation and lack of physical connections among the region's countries –a serious constraint to the integration process– CAF oriented its activities to those areas that could contribute to foster international connections, with particular emphasis on road construction, energy and telecommunications. Within the context of globalization characterized by competitiveness levels which call for an expansion of economic spaces, in line with the social and economic priorities of shareholder countries, CAF granted financing for public and private sector projects, including an economic evaluation of the projects, best practices in tender processes, project monitoring and the project finance modality.

The advantages offered by CAF –swift, client-oriented service, flexible in finding solutions, financing directly to subnational agencies without sovereign guarantee, and giving priority to integration projects– did not take long to bear fruit, and the growth of the infrastructure sector in the Corporation's portfolio, quickly reaching 70%.

**Approvals for infrastructure projects by quinquennium (1970-2005)** **US$ millions**



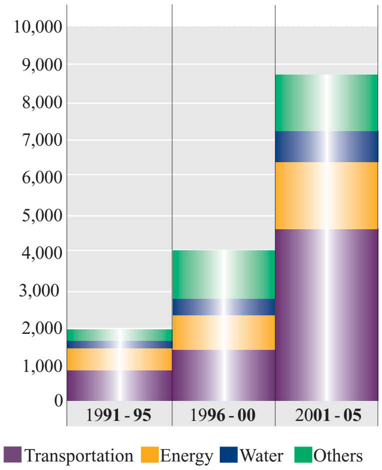

As of 2000, with the launching of the Initiative for Integration of South American Infrastructure (IIRSA) –which CAF helped to design–, the Corporation strengthened its support to the sector, increasing the resources in technical cooperation funds for evaluation studies and consulting services. The Corporation also started to finance large-scale, strong-impact projects for specific countries and the region as a whole. The percentage of CAF's portfolio earmarked for these projects continued to grow steadily on a yearly basis.

Also noteworthy are CAF's current actions to promote sustainable social development infrastructure, mainly in the areas of drinking water and basic sanitation facilities, rural development, health and education. Challenges are many and include increasing coverage and quality of social services, promoting infrastructure construction and productive financing at the rural level, assessing progress with respect to the UN's Millennium Goals, and fostering innovative mechanisms to take full advantage of social program's resources.

Since poverty and social exclusion is a multidimensional phenomenon, CAF applies a comprehensive strategy to earmark resources, in close collaboration with its shareholders . These strategies include: 1) support to the design of sectoral public policies based on sustainability, equity and pragmatism, strengthening national and local capacities; 2) priority to transparent and participative projects

**Approvals for infrastructure projects by sector**

US$ millions




that contribute to decentralization; and 3) co-financing programs leveraging resources while taking full advantage of the experiences and synergies among the various actors.

CAF used its broad experience and created in 2004 a unit promoting a technical dialogue with its shareholder countries on infrastructure at sectoral level. It disseminates information about best practices in relevant management and investment areas. Thus, the Corporation sponsors workshops and seminars in collaboration with the authorities in charge of the infrastructure sector in shareholder countries, publishes a series of bulletins on the status of this sector in each country, and has launched programs to improve performance in specific areas.

## Private sector: an engine for development

From its very creation, CAF has prioritized technical assistance and financing to the private sector –aware of its significant role in generating jobs and investments, promoting trade, consolidating markets, and contributing to transfer technology and knowledge. Technical assistance is also provided for high-impact projects –with increasing contributions to clean energy technologies and environmental protection– and programs to promote micro-, small- and medium-sized enterprises which intensively use and train labor force, thus helping to fight poverty and increasing living standards.

CAF's relations with the private sector are based on two fundamental principles: to complement markets' action and to serve as a catalytic agent for international financing and investment. CAF's work with this sector has long been guided by these two principles, which have helped the Corporation to evolve and meet the countries' major needs in each phase of their development processes.

During the 1980s, when shareholder countries practically had no access to international credits, CAF was among the few international financial institutions that were ready to finance foreign trade promotion in Andean countries. At that time, CAF focused on the financial sector –including development or second-floor banks and commercial banks– to underpin international trade flows in the productive sector.

Later on, with the end of the external debt crisis, the private sector started to have greater access to international credits, although they were granted mostly for foreign trade and short-term liquidity facilities, rather than short- and medium-term investments. This prompted CAF to focus on improving the private sector's productive capacity, financial profile and international insertion.

At present, CAF is directly or indirectly linked to all levels of the private sector, from large corporations to micro- and small enterprises, granting medium-term loans for large-scale projects and acting as a catalytic agent to attract additional resources through co-financing operations with official or multilateral institutions and international banks. The Corporation also provides credit lines to financial institutions that lend these funds to SMEs and Microfinance –a sector that also receives support through CAF's technical cooperation operations. Over the last few years, the Corporation has incorporated a number of innovative and competitive financial products and services, such as guarantees, equity investments, and banking investment and financial advisory services, among others (*pp. 117 to 119*).

CAF's catalytic role is also evidenced by its equity investments in various funds aimed at increasing foreign capital flows to shareholder countries and expanding their sources of financing. These funds are basically for promoting infrastructure projects –such as the Darby Latin American Mezzanine Fund and the Latin Power Fund, which finances electrical power projects in the region– or supports the business sector –as in the case of the Latin American Business Fund and the Latin American Investment Guarantee Company, which offers political risk insurance and investment guarantees to private financial institutions operating in the region.

In the area of co-financing, in 1997, CAF established its own A/B loan program. Thanks to its excellent credit ratings, the Corporation substantially improved its capacity to attract capital flows to support business initiatives. Under this modality, CAF has ensured the participation of 25 international

**In addition to its direct credits to the private sector, CAF offers entrepreneurs a broad variety of products, services and innovative financial mechanisms**

banks, concluding transactions for US$ 2,384 million, of which US$ 1,758 million came from international financial institutions.

At present, CAF also focuses on PPP projects (Public-Private Participation), taking advantage of its unique standing in both sectors and its experience in the area of infrastructure. Additionally, the Corporation supports financial sectors in shareholder countries, by using instruments aimed at improving their assets/liabilities ratio and expanding their sources of financing.

## The millenniun challenge: competitiveness

CAF's results demonstrate its added value, contributing to bolster its leadership in promoting economic and social transformations in the region. The Corporation has provided firm support to various efforts to improve competitiveness levels in Latin America –which are quite low mainly because of deficiencies in the areas of education, infrastructure, technology and institutionality. Thus, CAF pursues the goals of a more efficient and equitable insertion of the region into the global economy, poverty reduction and higher levels of development and well-being for the people.

CAF's commitment with shareholder countries has not limited financing to projects increasing competitiveness –as in the case of the resources earmarked for infrastructure and logistics– but it has been reinforced through various initiatives. For instance, with the CAF Competitiveness Program (PAC), CAF undertook the complex task of boosting competitiveness of its member countries more than five years ago, after signing an agreement with Harvard University in 1999. Its purpose is to develop a policy agenda for the public and private sectors, by making special emphasis on issues such as international trade, investment and macroeconomic framework, microeconomic bases for competitiveness, governance, environmental sustainability, science and technology.

On a second stage, PAC focused on designing and implementing projects a comprehensive vision. The program provided for research on the appropriate competitiveness strategies for countries rich in natural resources to maintaining their leadership. Five research studies and 38 projects were conducted in the Andean countries. They focused on cluster development, improvement of investment conditions, promotion of entrepreneurial capacities, information and communications technologies, knowledge assets, and institutional strengthening.

The PAC entered a third phase in 2005, by extending its coverage to non-Andean countries. It continued to promote competitiveness principles, helping economic agents to understand and adopt them, while promoting lasting changes in the way to create competitive enterprises and organizations.

CAF is also supporting first and second generation economic reforms in shareholder countries contributing to attain stability and creating the necessary conditions for growth, encouraging the private sector to expand itself while investing and producing with efficiency. CAF aims to develop and integrate market capitals in Latin America –particularly in the Andean region– which are characterized by relatively low levels of development, financial strength and market capitalization. These difficulties restrict opportunities to access larger and more efficient sources of financing for entrepreneurial investment and production, preventing the region from boosting competitiveness.

To face this problem, CAF created the Kemmerer Program in 1998 to contribute in markets development. The Program has succeeded in introducing best practices for corporate governance in the region's enterprises, in response to two major problems affecting the markets: the lack of transparency and weak corporate practices –as well as other factors such as macroeconomic instability and deficiencies in regulations, rule of law, and market monitoring institutions.

## Governance for greater social participation

For Latin America, globalization has entailed greater challenges in terms of its development, since the governments, the private sector and civil society have been required to play new roles to build a more equitable, participative and cohesive society with regional identity.

**In an effort to strengthen capital markets and ensure investments in Latin America, CAF is promoting the adoption of best practices for corporate governance by enterprises**

State reforms have been even more complex than economic reforms. In fact, progress in consolidating competitive economies cannot be made without establishing suitable state institutions. Another crucial requirement is to have a clear understanding among governments, the opposition, the private sector, civil society, labor, and international entities.

Aware of the need for the region to create the appropriate conditions to reach a balance among the various actors, gain civil society's confidence in authorities and institutions, and build social capital, CAF created the Governance Program in 2001, with four strategic action areas:

- Training in governance and political management.
- Integral support to municipal development in the Andean region.
- Program to create mechanisms to strengthen democratic governance and build consensus.
- Leadership for transformation.

Natural leaders who will reach out to their communities, adding to 1,600 citizens, have been trained in these areas, which are closely related to values, responsibility and relations management. Additionally, 320 citizens were trained in cadastral surveying and e-governance. Information about best practices was provided to over 15 municipalities in the Andean region.

## Technical cooperation and other specialized funds

Since its creation, CAF has supported shareholder countries through a key, multi-faceted operational modality called technical cooperation. Mandated in CAF's by-laws, this mechanism earmarks mostly non-reimbursable resources for crucial complementary activities. That is the case of CAF's support to reinforce the countries' technical capacity for preparing feasibility studies on projects with potentially high impact on their economies, sectoral studies on prioritize infrastructure works and consulting on integration-related issues, promoting regional tourism, and strengthening small- and mid-sized enterprises, in order to improve efficiency and competitiveness in both the public and private sectors.

### Other cooperation funds

**Special Fund for Bolivia (FEB) and Special Fund for Ecuador (FEE).** They were created in 1988 to offer technical assistance and satisfy the needs of the two relatively least developed countries in the Andean region. Both are contemplated by CAF's Constitutive Agreement.

**Andean Fund for Energy Conservation (FACE).** It provides resources for consulting and training in the area of energy sources conservation in Andean countries.

**Spanish Fund for Technical Cooperation and Canadian International Development Agency (CIDA).** Non-reimbursable financial resources under CAF administration, used to develop various sectors in strategic areas of top priority to CAF and the region such as institutional reform, infrastructure, energy, social development and environment protection.

**Funds managed for Germany's Kreditanstalt für Wiederaufbau (KfW).** Its resources are earmarked for consulting on integration projects in the neediest communities in CAF's member countries.

**Latin American Carbon Program (PLAC).** With projects for the reduction of greenhouse gases, this program supports shareholder countries' governments and private sectors participation in the carbon emissions reduction market.

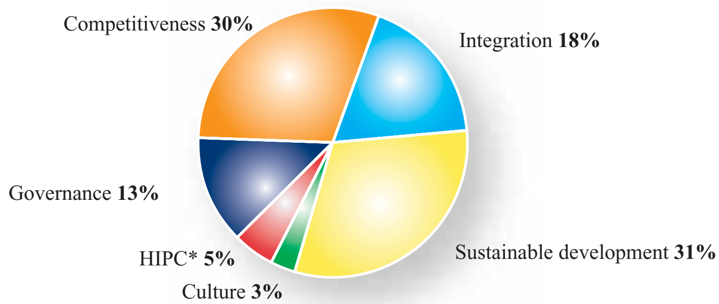
**Business Investment and Development Fund for Small- and Medium-Sized Enterprises (FIDE).** Strengthens equity capital of new or already established enterprises with projects for technological innovation and productive improvements, by investing in other funds supporting SMEs.

**Compensatory Financing Fund.** Provides non-reimbursable financing to partially cover costs of long-term loans granted to governments or State agencies for top-priority sectors to promote social development and integration in member countries.

Cooperation funds have been increasingly oriented to development and social programs, covering several areas: culture and community, training, competitiveness for social inclusion, micro- and small-sized enterprises, health and education, natural disaster relief, tourism and infrastructure, as well as musical education and sports programs for children and youngsters.

CAF also provides cooperation resources through the International Fund for Agricultural Development (IFAD) through projects enabling poor and indigenous communities in rural areas to access goods and services necessary to improve their productive work.

**Allocation of cooperation funds (1993-2005)**




* HIPC: Heavily Indebted Poor Countries

## Social and environmental agendas

As part of the strategies to promote sustainable development in the region, CAF prioritizes social and environmental challenges common to all Latin American countries: reducing poverty and social exclusion, promoting a more equitable income distribution, and protecting natural resources for future generations.

CAF has supported social development in its shareholder countries for over three decades. In the 1990s, it incorporated environmental protection and human and social development into its operational strategies and project assessment. CAF redefined its corporate mission to incorporate sustainable development as one of its fundamental pillars, leading to the creation of the first Sustainable Development Coordination Office in 1994. The number of projects including the concept of sustainable development increased notably in CAF's portfolio. The Corporation also continued its efforts to train staff and maintain its leadership in the area of sustainable development in the regional and international contexts.

In 1995, the Human Development Fund (Fondeshu) was created as a new mechanism for the region's sustainable development. The fund channels resources to fight social exclusion. Eventually, it formalized its support to micro-entrepreneurs by establishing an office in charge of financing micro-enterprises through intermediary institutions that offer direct loans to rural and urban micro-entrepreneurs. In 1998, it started a project to alleviate the impact of the El Niño phenomenon, which later became the Andean Program for Disaster Risk Prevention and Mitigation *(p.38*).

Later on, the Fund began to allocate resources for culture promotion in the region, establishing a symphonic orchestra with children and youngsters from underprivileged sectors in Andean countries. In expanding this initiative, the Program incorporated other activities that have successfully contributed to social and human development at the local, national and regional levels. Such growth prompted CAF to create the Direction of Cultural and Community Development, in charge of the Musical Education Program (covering instrumental, vocal and lutherie activities) and the Sports Education Program (as a tool for social development), along with a number of innovative, replicable and productive community projects, aimed at building capacity and promoting sustainable development in socially excluded communities.

## PREANDINO:

### An example of timely response from CAF to its shareholder countries

One of the main strengths of CAF is that it is capable of responding swift and timely to the requirements of its shareholder countries –which turns the Corporation into a reliable partner to resort to in difficult times. An example of this is the case of the Andean Program for Disaster Risk Prevention and Mitigation (PREANDINO), which was created as a CAF operational response to a request made by the XI Andean Presidential Council.
Its origin dates back to the year 1998, when the Andean Presidents gathered in Guayaquil, Ecuador, and entrusted CAF with the following tasks: studying the socio-economic impact of the natural disasters caused by the El Niño phenomenon; conducting an evaluation of the countries' institutional framework and management, and of the affected sectors; as well as proposing policies, strategies and projects for future reduction of negative consequences of these catastrophic natural events –which have caused great human and economic losses, as well as deterioration of the living standards in the affected regions. It should be noted that, during the 20th century, the El Niño phenomenon hit the region on twenty-two occasions, causing increasingly recurrent and tragic natural disasters.
Later on, the process to comply with the Presidential mandate led to the creation of PREANDINO, in charge of developing institutions and enforcing norms aimed at disaster risk prevention and the execution of regional projects identified as priorities.
It should be stressed that even before the creation of this program, CAF was already implementing actions and channeling resources towards initiatives in this area, including specific donations for humanitarian assistance in emergency cases.
A relevant contribution by CAF during this period was the publication of five books containing the lessons learned by the Andean countries –Bolivia, Colombia, Ecuador, Peru and Venezuela– in the wake of the El Niño phenomenon, which strongly affected these countries in 1997 and 1998. Each book includes in-depth studies of the socio-economic impact of El Niño, which are still valid in view of the recurrence of the phenomenon. The analyses cover the effects at the levels of provinces and hydrographic basins, the chain of impacts on the various economic sectors, the judicial and institutional frameworks to cope with disasters, and the policies aimed at reducing vulnerability.
Since its creation in December 2000, this program has made important achievements, including the following:
At the regional level, progress was made towards the creation of mechanisms to support the working PREANDINO Network which, based on the institutional frameworks of the countries, incorporated 340 institutions with the direct participation of 1,703 professionals. The program team also participated in the creation of the Andean Committee for Disaster Prevention and Assistance (CAPRADE) within the context of the Andean Integration System and the Andean Strategy for Disaster Prevention and Assistance, and contributed to obtain resources of € 12 million from the European Union to support its consolidation.
Similarly, the program team held four meetings at the regional level, with the participation of 385 delegates representing the countries' institutions. In these three-day events, the Andean countries submitted reports on the progress achieved in modernizing the legal and institutional frameworks that support and foster risk management, as well as the inclusion of elements for risk prevention and reduction in the planning mechanisms.
In addition, they agreed on actions for mutual support which were included in four plans for horizontal cooperation.
Support was also given to the formation of working networks with the agencies in charge of scientific knowledge in the region, so as to create the regional platform of the International Research Center on El Niño (CIIFEN) and financing was provided for an organizational study and an action plan to consolidate the platform.
At the level of the various countries in the region, PREANDINO helped them to make progress towards the institutionalization of risk management through the following processes:

- Promotion or strengthening of the institutional framework for risk management.
- Incorporation of risk management into development planning.
- Awareness raising and promotion of a preventive culture.
- Gathering and systematization of information, and promotion of the development of scientific knowledge on dangers, vulnerabilities and risks.

In mid-2005, the first stage of the program came to an end.
At present the program team is planning to further promote the institutional strengthening process, so that national entities in charge of planning can fully assume the responsibility of following up the lines of work.

**CAF attaches importance to macroeconomic stabilization processes as they allow for meeting people's needs and attaining the countries' social and environmental goals**

In 2004, as a result of an internal process to increase efficiency in meeting shareholder countries' requirements in a systematic way while optimizing social, environmental and SMEs and Microfinance investments, CAF created its Direction for Social and Environmental Development, thus incorporating the Directions for Environment, for SMEs and Microfinance, and Social Development. CAF has various operational modalities and financial sources for activities in these areas. For instance, it has supported social development in shareholder countries mostly through multisectoral loans.

CAF has also broadened its environmental agenda from its initial evaluation and follow-up tasks to include support to shareholder countries in regional policy-making, institutional and regulatory strengthening, and design of innovative projects. CAF's environmental protection efforts are supported by several information systems and strategic programs: the Latin American Carbon Program (PLAC), the Biodiversity Program (BioCAF), the Sustainable Development Program for Financial Institutions, and PREANDINO, which are aimed at contributing to member countries' insertion into the competitive carbon market, supporting the conservation of biodiversity and biotrade, fostering sustainable development in the region's financial sector, and promoting the reduction of natural disaster risks, respectively.

Traditionally, CAF has assigned priority to supporting micro-, small- and mid-sized enterprises by granting loans to public and private financial institutions focusing on these segments. At present, the Corporation also offers a wide variety of business initiatives through financial mechanisms tailored to the needs of targeted sectors (*p. 103*). With approvals of over US$ 60 million, CAF has consolidated micro-finance institutions that provide resources to micro-enterprises.

## Financial Indicators: sustained, high-quality growth

CAF's assets have increased steadily since 1980 thanks to the continued expansion of its loan portfolio and the overall economic growth in the region's countries, reaching an average annual rate of 19% during the period 1970-2005 and amounting to over US$ 9,541 million by the end of 2005. Such growth has reinforced the Corporation's capacity to finance sustainable development and regional integration projects in shareholder countries.

Conservative management and strict compliance with credit policies have been fundamental to CAF's success. In pursuing its regional economic development goals, the Corporation follows traditional banking practices for loan approvals and thorough procedures for risk management. As a result of this policy –as well as the macroeconomic progress in shareholder countries and their preferential treatment– CAF has operated with minimum operating loss margins in its loan portfolio since its very creation. The percentage of non-performing loans in CAF's portfolio has traditionally been very small, representing only 0.02% at the end of 2005.

Over the last 25 years, CAF has experienced sustained equity growth as a result of its policy of retaining most of its earnings and the regular increases in its paid-in capital. CAF's subscribed capital –which presently exceeds US$ 1,230 million– has been increased on several occasions, most recently in 1999, 2001, 2002, 2003, 2004 and 2005. Also noteworthy is the fact that, when it became a shareholder in 2002, Spain made a substantial payment in subscribed callable capital (US$ 200 million), which further improved the Corporation's credit rating.

CAF has consistently reported positive net earnings since 1975, reaching US$ 283 million in 2005, with an average inter-annual growth rate of approximately 20% in the last 10 years.

## Standing in international financial markets

CAF has made significant changes in its strategy to attract resources. Until the 1990s, the Corporation operated mainly with capital provided by its shareholders and external resources generally stemming from short-term loans. As of 1992, however, CAF adopted a financial strategy to diversify financial

## The history of a successful issuer

To become a successful issuer in the main international capital markets and, furthermore, to keep such a position for years, is not an easy task for a financial institution based in Latin America –since it is a very vulnerable region to the ups and downs of the global economy which is often affected by the scarcity of foreign capital flows.

Nevertheless, success in this area has been one of the major achievements of CAF, which now enjoys access to medium- and long-term institutional investors in the United States, Europe, Japan and Asia. This is a crucial achievement, not only because it allows the Corporation to obtain resources in competitive conditions and to make them available for development projects in its shareholder countries, but also because it strengthens Latin American presence in those markets.

Since CAF was granted investment-grade ratings for its issues by three world-famous credit rating agencies, the Corporation's ratings have been periodically upgraded thanks to its steady and strong operational results, its careful handling of its credit portfolio and its sound financial policies. Along with the support of its shareholder countries, this has earned the Corporation international recognition as a lending institution with a very low credit risk and a strong presence in international capital markets, with 49 security issues over the past 12 years accounting for more than US$ 7,000 million.

### Evolution of CAF's risk ratings

**1993** CAF obtains three *investment-grade ratings* for its long-term debt bonds denominated in foreign currency from the most renowned rating agencies of the world: *Baa3* from Moody's Investors Services, *BBB* from Standard & Poor's, and *A-* from Fitch. It becomes the first Latin American issuer to obtain these ratings simultaneously.

**1995** CAF is awarded the prize "Best Issuer in Latin America", granted by the European magazine *Euromoney*, and becomes the first Latin American issuer to gain access to international financial markets after the Mexican financial crisis. In addition, Fitch and Standard & Poor's reiterate their risk ratings, while Moody's approves an upgrade of its rating effectively as of January 1996.

**1996** Risk ratings for CAF's long-term debt bonds are upgraded. Moody's does it in January (from Baa3 to *Baa2*) and Standard & Poor's in November (from BBB to *BBB+*). Both agencies also assign a risk rating to the Corporation's short-term debt bonds (*P-2* and *A-2*, respectively).

**1997** In June, Moody's upgrades its investment rating of CAF's long-term debt bonds from Baa2 to *A3*, the highest rating ever assigned by this agency to a Latin American institution.

**1998** In spite of the global financial crisis, CAF's excellent ratings are ratified by the three agencies during this year, thus helping the Corporation to maintain its leading position in international capital markets. CAF becomes the first Latin American issuer to have access to these markets after the financial crises in Asia and Russia, thereby restoring invertors' confidence in the region.

**1999** In August, Standard & Poor's upgrades its risk rating from BBB+ to *A* for CAF's long-term debt bonds and from A-2 to *A-1* for short-term bonds. CAF becomes the best-rated issuer in Latin America.

**2000** Fitch increases its ratings for CAF's long-term and short-term debt issues from A- to *A* and from F2 to *F1*, respectively, and the Corporation maintains its position as best-rated issuer in Latin America. This year, the *Latin Finance* magazine awards CAF the "Prize to the Best Multilateral Institution of the year 2000" in recognition of its performance as issuer and catalytic agent during the period, and of its work during its three decades of existence.

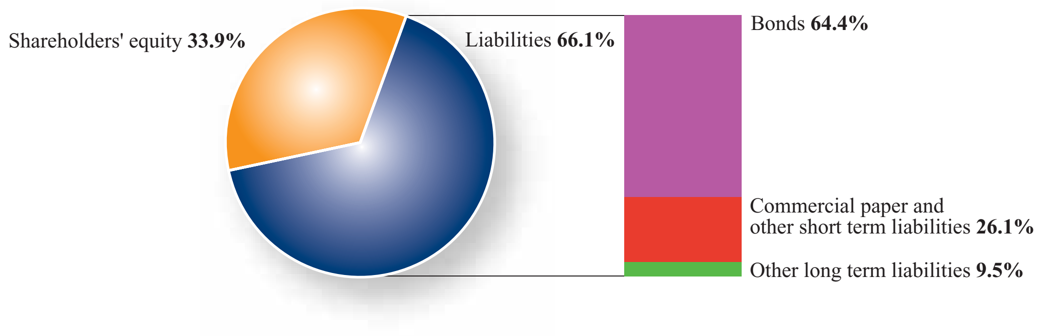
**2001** In May, Moody's upgrades its ratings of CAF's long-term and short-term debt issues from A3 to *A2* and from P2 a *P1*, respectively. Once again, CAF turns out to be the best-rated Latin American issuer.

**2003** CAF receives three prizes for its performance in the most demanding financial markets of the world: "Issuing Agency of the Year", "Best Bond Issue for Financing Development" and "Best Multilateral Institution" from the specialized magazines *Euromoney*, *Emerging Markets* and *Latin Finance*, respectively.

**2004** During this year, CAF is awarded once again the same three prizes it received the previous year. In addition, all the agencies evaluating the Corporation reiterated their ratings, thus allowing it to maintain its position as a frequent issuer with the highest ratings in Latin America.

**2005** Moody's further upgrades its rating of CAF's long-term issues from A2 to *A1*. In addition, the Japanese agency Japan Credit Rating (JCR) assigns for the first time ever its highest risk rating to a Latin American institution, by grading CAF's long-term debt issues as *AA-*.

**Sources of financing (At December 31, 2005)**




sources, reduce costs and minimize risks associated with currency and interest rate fluctuations, thereby reinforcing its catalytic power to attract and allocate resources to operations in member countries in a competitive way.

At present, CAF obtains nearly 90% of its resources from extra-regional sources, including international banks, government agencies in developed countries and multilateral financial organizations. CAF marked a milestone when it became the first Latin American issuer to simultaneously receive investment grade ratings from Standard & Poor's, Moody's Investors Service and Fitch in 1993. Since then, CAF has turned itself into a renowned and versatile financial institution, by increasing its capacity to attract resources through mid- and long-term issues in international bond markets –particularly in Europe, Japan and the United States.

Thanks to its consistent financial strength, shareholders' support, cautious credit management and policies, and political independence, CAF has become the best-rated frequent-issuer in Latin America including, more recently, *AA-* from Japan Credit Rating Agency (*previous page*). This has allowed CAF to issue bonds in international capital markets under increasingly competitive conditions. Between 1993 and 2005, the number of issues rose to 49 for a total amount of US$ 7,103 million. These issues have been placed in the United States, Europe and Japan, and in some regional markets, in different currencies and with maturity terms of up to 20 years.

It should be noted that CAF also operates in short-term capital markets through various commercial paper issuance programs in the United States (US$ 1,000 million) and Europe (US$ 500 million), and a short-term note program in Spain (€ 500 million).

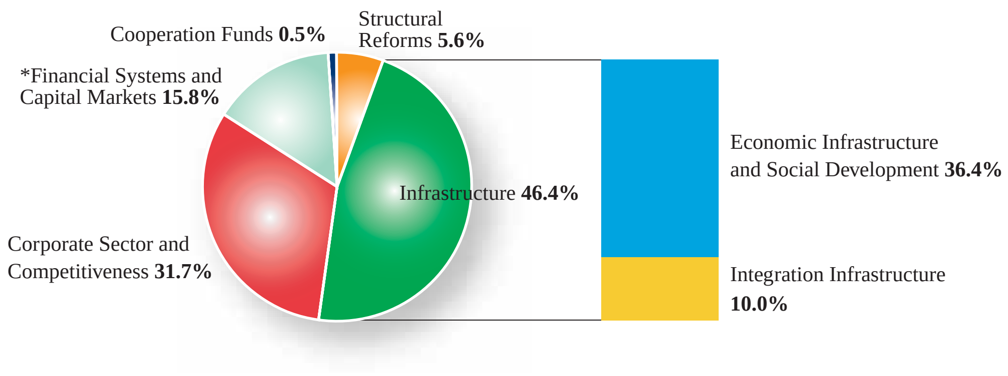
## Institutional growth for successful competition

CAF has shown sustained institutional growth in providing financial services and mechanisms to private and public sector clients in its shareholder countries.

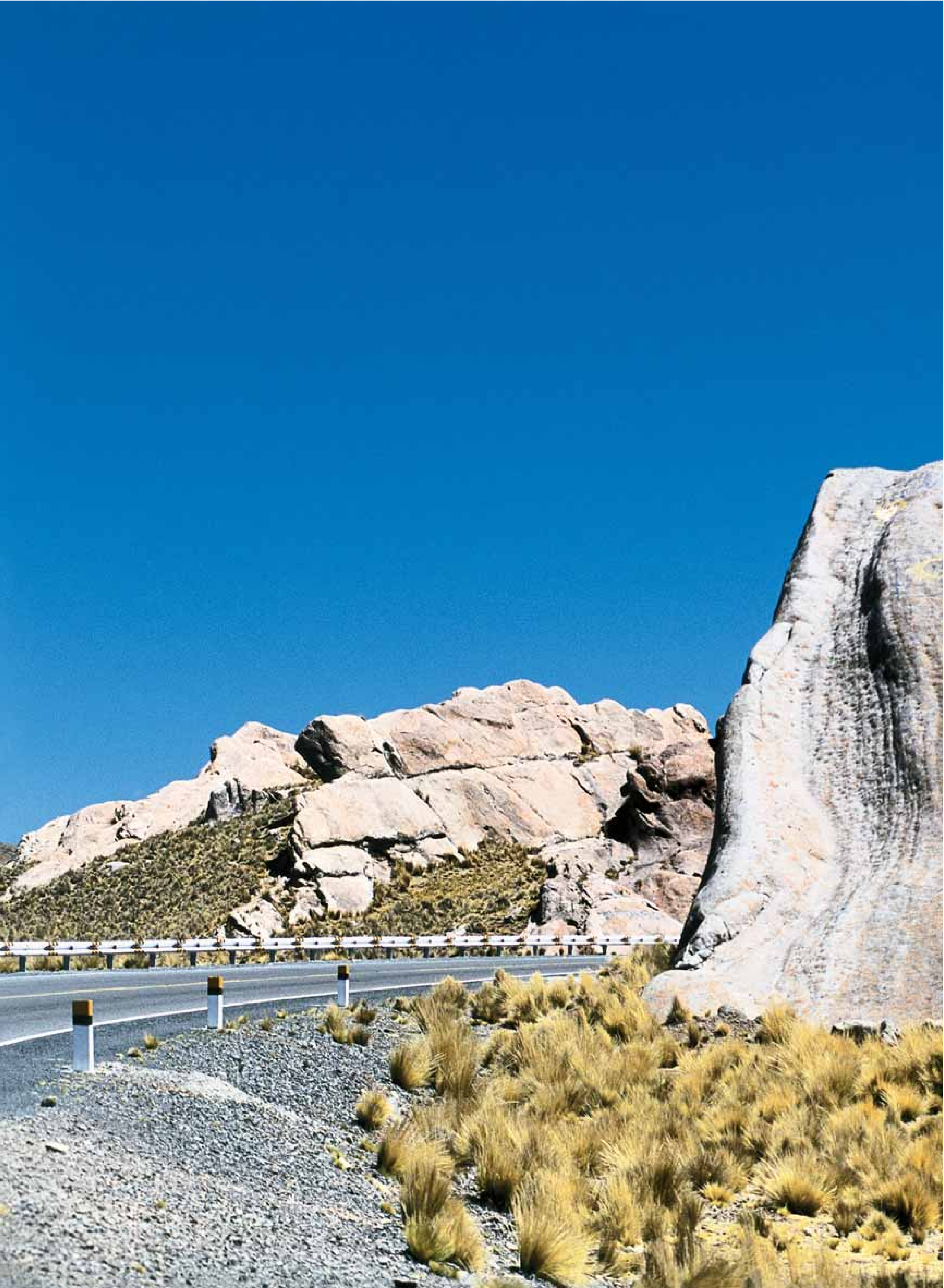
Thanks to several organizational adjustments over the past few years, CAF's structure has been regularly updated and modernized on the basis of client-oriented business processes and institutional strengthening, in line with its strategic model. In this way, it ensures corporate sustainability in the medium and long term, adapting itself and responding to the changing needs of shareholder countries, markets and the international scene, while timely offering top-quality products and services to all the markets where it operates.

As a result of its institutional strengthening, CAF has turned itself into a solid international financial corporation with a sound loan and investment portfolio aimed at clients in both the public and private sectors, and a strong impact on the development of its shareholder countries and the Latin American integration process. Thus, CAF is an increasingly important source of financing for productive investment in key strategic sectors for development, providing vital support to economic, social and environmental projects.

**Approvals by strategic sectors 1990-2005**




* Includes SMEs and Microfinance




GLORIA
SUPERVISOR

# Financial and operational analysis

# Operations

## 1. Approvals

CAF'S ACTIVITIES FOR 2005 were based on improved economic projections for Latin America and an expected growth rate of 4.3% in the Andean economies, as a result of positive performances by the export sectors. These expectations were surpassed, as growth reached 6.7% based on preliminary data for the year.

CAF's approvals totaled US$ 4,746 million in 2005 (*Table N° 1*) reflecting a year to year increase of 35%, and reaffirming its reliability in responding to the financial needs of its clients, both public and private. Direct approvals were 26% higher than last year's, and catalytic approvals also experienced a substantial increase to US$ 505 million as the Corporation's initiatives attracted other sources of financing from institutions interested in participating with CAF in financing important projects to promote the region's economic development.

Table Nº 1

**Approvals by country** — **In US$ millions**

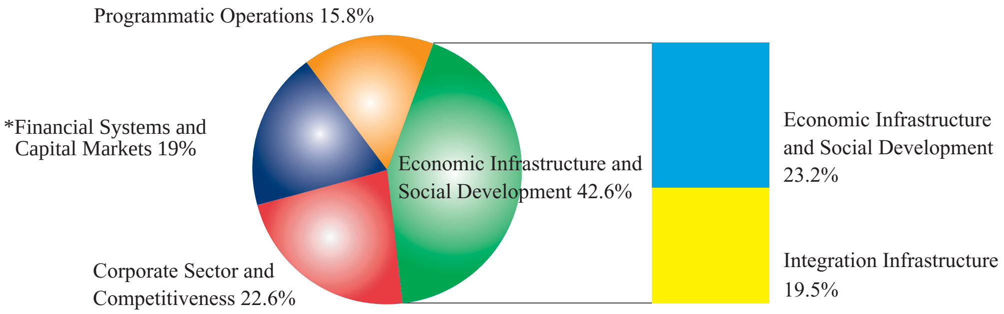
| Country | 2001 | 2002 | 2003 | 2004 | 2005 | 2001-05 |
|---|---|---|---|---|---|---|
| Bolivia | 464 | 503 | 619 | 499 | 523 | 2,608 |
| Colombia | 819 | 750 | 617 | 922 | 1,237 | 4,344 |
| Ecuador | 356 | 407 | 438 | 338 | 815 | 2,355 |
| Peru | 650 | 498 | 633 | 604 | 417 | 2,801 |
| Venezuela | 738 | 762 | 535 | 821 | 627 | 3,484 |
| Argentina | - | - | 175 | 60 | 257 | 493 |
| Brazil | 112 | 260 | 245 | 170 | 695 | 1,482 |
| Costa Rica | - | - | 30 | 63 | 2 | 94 |
| Mexico | 33 | 2 | 2 | 2 | 5 | 43 |
| Panama | - | - | - | 1 | 80 | 81 |
| Paraguay | 2 | - | - | 11 | 11 | 24 |
| Uruguay | - | 100 | - | - | 70 | 170 |
| Others | 22 | 9 | 9 | 13 | 7 | 61 |
| **Total** | **3,197** | **3,290** | **3,303** | **3,503** | **4,746** | **18,039** |

Significant amounts were approved for non-Andean countries (US$ 1,127 million), equivalent to 24% of total approvals, reflecting the importance which CAF assigns to the economic integration of sectors that are essential for the development of the region.

42.6% of the Corporation's approvals targeted economic infrastructure and social development projects, 19.5% of which corresponded to integration infrastructure. Financing was also approved to various initiatives in productive sectors (22.6%) as well as to SMEs and Microfinance through the financial systems (19%). In addition, resources were approved to support macroeconomic stabilization programs and important structural reforms carried out by shareholder countries (*Graph N° 1*).

Graph N° 1

**Approvals by Strategic Sectors**




* Includes SMEs and Microfinance

## Approvals by tenor

In line with CAF's commitment to sustainable development and regional integration, long-term loans continued to dominate the Corporation's total approvals in 2005. This commitment is confirmed by the fact that approvals having a tenor of 10 or more years amounted to 64% of the total operations. This figure is of particular importance in view of CAF's increase participation in private sector initiatives, both directly as well as through joint participation with the public sector, reflecting a strong institutional incursion into segments that can contribute significantly to improving the countries' economic conditions. The increase in medium-term operations –5 to 10 years– whose relative share grew from 2% in 2004 to 18% in 2005 was also significant (*Graph N° 2* and *Table N° 2*).

Graph N° 2

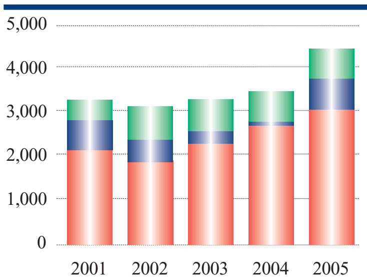



Table N° 2

**Approvals by tenor** In US$ millions

| | 2001 | 2002 | 2003 | 2004 | 2005 | 2001-05 |
|---|---|---|---|---|---|---|
| Long-term loans | 2,020 | 1,920 | 2,202 | 2,682 | 3,049 | 11,872 |
| Medium-term loans | 795 | 625 | 218 | 62 | 876 | 2,576 |
| Short-term loans | 383 | 745 | 884 | 758 | 822 | 3,591 |
| **Total** | **3,197** | **3,290** | **3,303** | **3,503** | **4,746** | **18,039** |

## Approvals by risk category

As the result of a more stable environment in the region, characterized by a solid economic performance, attractive private sector initiatives were supported in 2005, and contributed to a substantial increase in the relative share of non-sovereign risk operations in the Corporation's approvals (*Table N° 3*). Although, these operations totaled US$ 2,245 million (*Graph N° 3*), sovereign risk operations continued to be predominant and accounted for more than 53% of the total approvals by CAF.

Graph N° 3

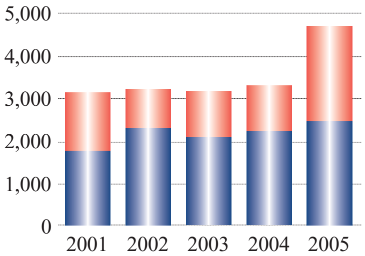



Table N° 3

**Appovals by risk category** **In US$ millions**

| | 2001 | 2002 | 2003 | 2004 | 2005 | 2001-05 |
|---|---|---|---|---|---|---|
| Sovereign | 1,841 | 2,385 | 2,166 | 2,330 | 2,501 | 11,224 |
| Non-sovereign | 1,356 | 905 | 1,137 | 1,172 | 2,245 | 6,815 |
| **Total** | **3,197** | **3,290** | **3,303** | **3,503** | **4,746** | **18,039** |

## Approvals by economic sectors

As observed in *Table N° 4*, in 2005 approvals in the Transportation, Warehousing and Telecommunications, Electric Power, Natural Gas and Water supply sectors continued to have important weight. Indeed, 62% of totals approvals (US$ 2,301 million) were destined for projects to improve communications infrastructure and to provide greater access to basic social services for low income sectors, thus laying the foundations to boost competitiveness levels in the region.

Table N° 4

**Approvals by economic sector** **In US$ millions**

| Economic sector | 2001 | 2002 | 2003 | 2004 | 2005 | 2001-05 |
|---|---|---|---|---|---|---|
| Agricultural Infrastructure | 84 | 80 | 51 | - | - | 215 |
| Exploitation of mines and quarries | - | - | 30 | - | 50 | 80 |
| Manufacturing | 513 | 22 | 281 | - | 446 | 1,262 |
| Electric power, natural gas and water supply | 618 | 769 | 380 | 626 | 674 | 3,066 |
| Transportation, warehousing and communications | 672 | 1,103 | 1,287 | 1,189 | 1,628 | 5,879 |
| Whosale and retail trade | - | - | - | - | - | - |
| Public sector administration | 195 | - | 172 | 735 | 700 | 1,802 |
| Hotels and restaurants | 18 | 20 | - | 2 | - | 40 |
| Financial intermediation | 370 | - | - | - | 10 | 380 |
| Other social services and public health | 296 | 369 | 271 | 199 | 125 | 1,260 |
| Education | 57 | 167 | 40 | - | 55 | 319 |
| **Total** | **2,823** | **2,529** | **2,512** | **2,751** | **3,687** | **14,303** |

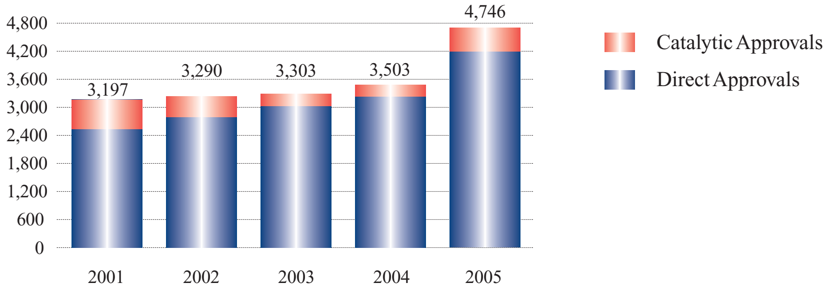
Of particular significance are the road and integration corridors supported in Argentina, Bolivia, Colombia, Ecuador, Panama, Paraguay and Peru, as well as the construction and improvement of mass transportation networks in Venezuela. As regards the supply of basic services, investment programs in water supply, basic sanitation and irrigation projects in Colombia, Ecuador and Venezuela were financed. Support was also provided to important investment programs in the education sector in Colombia, Ecuador and Venezuela, as well as to energy infrastructure in Bolivia, Brazil, Colombia and Ecuador.

### Catalytic role

In compliance with one of the pillars of CAF's corporate mission –playing a catalytic role in providing financing to the region– accumulated approvals associated with these activities that complement CAF's direct financing operations totaled over US$ 2,300 million during the past five years (*Graph N° 4*).

Graph N° 4

**Catalytic participation in approvals** **In US$ millions**




CAF's financial participation facilitated the region's access to other sources of international financing in the amount of US$ 505 million during 2005, especially through A/B loans and credit guarantees to both public and private sector entities.

Table N° 5

**Composition of financing for projects and corporate loans** **In US$ millions**

| Financing source | 2001 | 2002 | 2003 | 2004 | 2005 |
|---|---|---|---|---|---|
| CAF lending | 2,373 | 2,121 | 2,359 | 2,542 | 3,221 |
| Clients contributions | 1,332 | 752 | 3,095 | 3,087 | 1,559 |
| Other local sources | 675 | 92 | 1,037 | 680 | 1,779 |
| Extra-regional sources | 1,154 | 624 | 3,191 | 2,650 | 1,802 |
| • International lending institutions | 152 | 146 | 1,625 | 1,453 | 583 |
| • Other external sources | 1,002 | 478 | 1,565 | 1,198 | 1,219 |
| Total project cost | 5,534 | 3,589 | 9,683 | 8,959 | 8,362 |
| CAF lending as percentage of total cost | 43% | 59% | 24% | 28% | 39% |

From another perspective, in 2005 CAF participated more actively in the financing of projects, as indicated by its lending as percentage of their total cost which rose to 39% and amounted to US$ 3,221 million (*Table N° 5*); this represented an increase of over 26% in comparison with the previous year. In addition, CAF participated in longer-term and larger projects, which required the participation of other sources of financing from within and outside the region.

## 2. Disbursements

In 2005, CAF disbursed US$ 2,337 million, including the B tranches of A/B loans (*Table N° 6*). Of total disbursements during the year, 76% (US$ 1,772 million) were destined to Andean Community Countries. As part of its efforts to contribute to the region's integration, the Corporation substantially increased the amount of resources provided to non-Andean countries (24%). With these disbursements the Corporation materializes its commitments to projects and programs, and to its clients, and contributes towards a more equitable and inclusive development of the region.

Table Nº 6

**Disbursements by country** — In US$ millions

| Country | 2001 | 2002 | 2003 | 2004 | 2005 | 2001-05 |
|---|---|---|---|---|---|---|
| Bolivia | 271 | 365 | 346 | 258 | 280 | 1,520 |
| Colombia | 379 | 591 | 325 | 647 | 688 | 2,630 |
| Ecuador | 371 | 221 | 359 | 298 | 340 | 1,590 |
| Peru | 695 | 413 | 267 | 465 | 256 | 2,096 |
| Venezuela | 719 | 311 | 337 | 309 | 208 | 1,885 |
| Other countries | 112 | 284 | 145 | 52 | 565 | 1,159 |
| **Total** | **2,548** | **2,186** | **1,780** | **2,029** | **2,337** | **10,879** |

## 3. Portfolio

CAF's total investment and loan portfolio –which includes its equity investments and loans, the co-financed portion of its portfolio and loans guaranteed by its partial credit guarantee program– reached a combined total of US$ 8,082 million at end 2005, representing an increase of 4% with respect to 2004 and maintaining the steady growth trend of the last few years (*Graph N° 5* and *Table N° 7*).

Graph N°5

**Total portfolio*** — In US$ millions

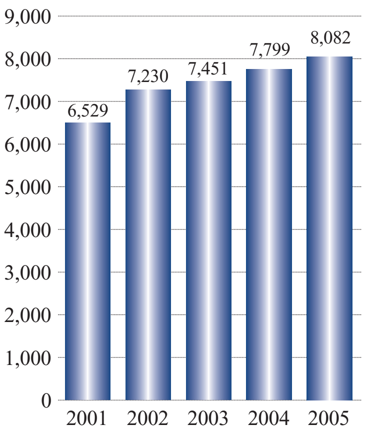



Table Nº 7

**Total portfolio *** — In US$ millions

| | 2001 | 2002 | 2003 | 2004 | 2005 |
|---|---|---|---|---|---|
| **Subtotal CAF's direct portfolio** | 5,575 | 6,180 | 6,712 | 7,216 | 7,462 |
| • CAF's loan portfolio | 5,455 | 6,062 | 6,597 | 7,104 | 7,347 |
| • Equity investments | 120 | 117 | 115 | 112 | 115 |
| **Subtotal catalytic component** | 954 | 1,051 | 738 | 583 | 620 |
| • Loan portfolio under CAF's administration | 700 | 647 | 409 | 280 | 419 |
| • Equity investments under CAF's administration | 4 | 4 | 4 | 3 | 3 |
| • PCG-related portfolio | 250 | 400 | 325 | 299 | 199 |
| **Total CAF portfolio** | **6,529** | **7,230** | **7,451** | **7,799** | **8,082** |

* Includes the co-financed component of CAF's portfolio and credits obtained through CAF's partial credit guarantee program.

## Total portfolio by country

At the end of 2005, over 89% of CAF's total portfolio was invested in Andean Community countries, while the remaining 11% included operations in other shareholder countries and regional operations, as shown in *Table N° 8*.

Table N° 8

**Total portfolio* by country** — In US$ millions

| Country | 2001 | 2002 | 2003 | 2004 | 2005 |
|---|---|---|---|---|---|
| Bolivia | 581 | 703 | 883 | 962 | 1,125 |
| Colombia | 1,835 | 2,122 | 1,991 | 2,112 | 1,985 |
| Ecuador | 1,120 | 1,122 | 1,209 | 1,226 | 1,231 |
| Peru | 1,112 | 1,299 | 1,403 | 1,664 | 1,724 |
| Venezuela | 1,406 | 1,348 | 1,289 | 1,219 | 1,137 |
| Other countries | 475 | 637 | 676 | 616 | 879 |
| **Total** | **6,529** | **7,230** | **7,451** | **7,799** | **8,082** |

* Includes the cofinanced component of CAF's portfolio and credits obtained through CAF's partial credit guarantee program.

## Portfolio according to operational modality

As reflected in *Table N° 9*, the long-term portion of CAF's portfolio –mostly in long-maturing infrastructure and social development projects and programs– continued to grow in 2005, reaching US$ 7,568 million, while the medium-term portfolio declined and the short-term portfolio increased substancially.

Cuadro Nº 9

**Total portfolio* by operational modality** — In US$ millions

| Operational modality | 2001 | 2002 | 2003 | 2004 | 2005 |
|---|---|---|---|---|---|
| Equity investments portfolio | 124 | 121 | 119 | 116 | 117 |
| Long-term loans | 5,560 | 6,151 | 6,444 | 7,041 | 7,568 |
| Medium-term loans | 583 | 763 | 748 | 493 | 57 |
| Short-term loans | 263 | 195 | 139 | 150 | 339 |
| **Total** | **6,529** | **7,230** | **7,451** | **7,799** | **8,082** |

* Includes the cofinanced component of CAF's portfolio and credits obtained through CAF's partial credit guarantee program.

## Total portfolio by risk factor

83% of CAF's total portfolio for 2005 (US$ 6,726 million) was comprised of loans in the sovereign risk category (*Table N° 10*), while non-sovereign loans accounted for 17% (US$ 1,356 million) of the total, reflecting the Corporation's commitment to its shareholders and principal clients. It should be noted that certain sovereign risk operations that are channeled through public entities, such as development banks and similar organizations, are in fact to on-lent micro, small and medium-sized private sector enterprises.

Table N° 10

| Total portfolio* by risk factor | | | | | In US$ millions |
|---|---|---|---|---|---|
| | **2001** | **2002** | **2003** | **2004** | **2005** |
| Sovereign risk | 4,777 | 5,719 | 6,315 | 6,855 | 6,726 |
| Non-sovereign risk | 1,752 | 1,512 | 1,136 | 944 | 1,356 |
| **Total** | **6,529** | **7,230** | **7,451** | **7,799** | **8,082** |

* Includes the cofinanced component of CAF's portfolio and credits obtained through CAF's partial credit guarantee program.

## Total portfolio by economic sector

As shown in *Table Nº 11*, in 2005 the infrastructure sector continued to have the highest priority in the member countries and the largest level of support from CAF. Specifically, the proportion of the portfolio dedicated to "Transportation, Warehousing and Communications" and to "Electric Power, Natural Gas and Water supply" represent nearly 50% of CAF's total portfolio, while the "Education, Social and Health Services" sector is second in importance with 21% of the portfolio.

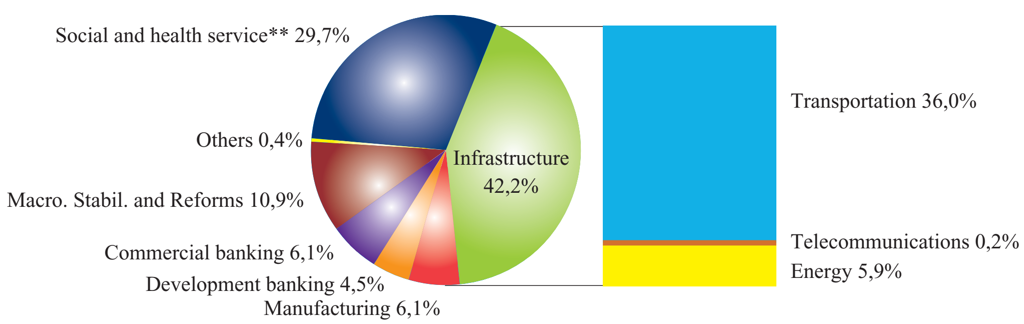
Table N° 11

| Total portfolio* by economic sector | | | | | In US$ millions |
|---|---|---|---|---|---|
| **Economic sector** | **2001** | **2002** | **2003** | **2004** | **2005** |
| Agricultural infrastructure | 201 | 344 | 293 | 271 | 220 |
| Exploitation of mines and quarries | 0 | 4 | 34 | 13 | 10 |
| Manufacturing | 690 | 511 | 307 | 278 | 491 |
| Electric power, natural gas and water supply | 1,396 | 1,624 | 1,454 | 1,015 | 928 |
| Transportation, warehousing and communications | 1,525 | 2,023 | 2,597 | 2,942 | 2,930 |
| Commercial banking | 735 | 522 | 319 | 395 | 493 |
| Development institutions | 611 | 595 | 534 | 346 | 365 |
| Education, social and health services | 561 | 1,542 | 1,444 | 1,879 | 1,729 |
| Other activities | 810 | 66 | 469 | 659 | 916 |
| **Total** | **6,529** | **7,230** | **7,451** | **7,799** | **8,082** |

* Includes the cofinanced component of CAF's portfolio and credits obtained through CAF's partial credit guarantee program.

Graph Nº 6

**Total portfolio* by economic sector** — **As of December 31, 2005**




* Includes third-party portfolio, managed and administered by CAF, as well as loans associated with partial credit guarantees.

** Includes Water, Sanitation, Education and other Social and Health Services, as well as the portfolio related to Social Infrastructure.

## Equity investments

By the end of 2005, CAF's equity investment portfolio totaled US$ 117 million and consisted of 27 direct capital investments, specially in funds specialized in diverse economic sectors such as infrastructure, SMEs and microfinance. Such investments will continue in the future using very selective criteria based on their alignment with CAF's objectives, the quality of the administrators and a rigorous risk analysis. Greater participation is anticipated in financing small and medium-sized enterprises through the Business Investment and Development Fund (FIDE).

Table N° 12

**Total equity investment portfolio** — In US$ millions

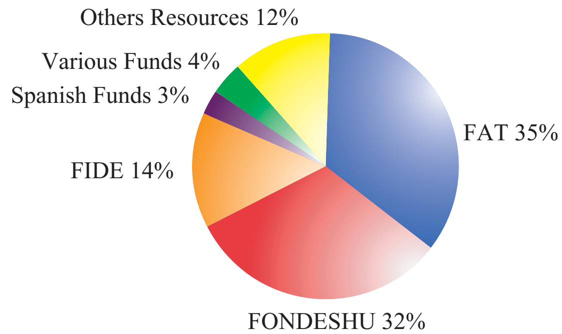
| Country | 2001 | 2002 | 2003 | 2004 | 2005 |
|---|---|---|---|---|---|
| Bolivia | 9 | 10 | 10 | 8 | 8 |
| Colombia | 2 | 2 | 2 | 1 | 1 |
| Ecuador | 1 | 1 | 1 | 1 | 1 |
| Peru | 23 | 16 | 14 | 12 | 10 |
| Venezuela | 2 | 2 | 0 | 0 | 0 |
| Other countries | 87 | 89 | 92 | 93 | 96 |
| **Total** | **124** | **121** | **119** | **116** | **117** |

## 4. Technical cooperation and other grant operations

Cooperation funds include off-balance resources assigned from the Corporation's net earnings and third-party resources under CAF's administration. They include the Technical Assistance Fund (FAT), the Human Development Fund (Fondeshu), the Latin American Carbon Program (PLAC), the Business Investment and Development Fund (FIDE), the Spanish Funds for Technical Cooperation, the Andean Fund for Energy Conservation (FACE) and the Kreditanstal für Weideraufbau (KFW), as well as the Special Funds for Bolivia and Ecuador and funds assigned to the HIPC Program (Heavily Indebted Poor Countries).

Graph Nº 7

**Origin of funds for technical cooperation and other grant operations*** — As of December 31,2005



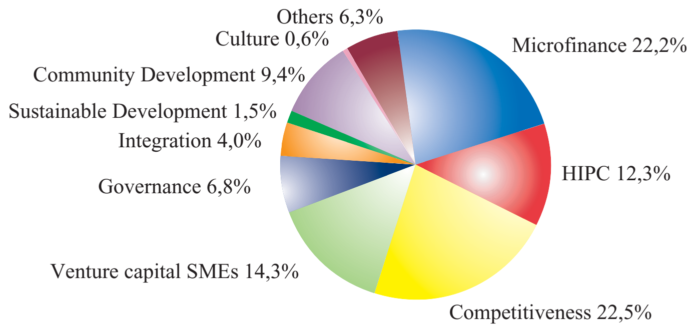

* Includes operations with reimbursable resources from FONDESHU and FIDE

In 2005, CAF's approvals with these funds totaled US$ 31.5 million. As shown in *Graph N° 7*, the Technical Assistance Fund (FAT) represented the largest share, with 35% of total operations and activities amounting to US$ 11 million. FIDE and Fondeshu were next with a joint share of 46% of the funds, or contributions amounting to US$ 4.5 million and US$ 9.9 million, respectively, followed by "other resources", directly assigned to the HIPC Initiative with 12% of the total (US$ 3.9 million). The remaining 4%, representing US$ 1.1 million, includes operations with the Special Funds for Bolivia and Ecuador, the FACE, the Latin American Carbon Program and operations financed with the Spanish Cooperation Funds, supporting various initiatives for approximately US$ 0.9 million.

*Graph N° 8* shows the use of cooperation funds by type of activity. Cooperation resources are mainly used in activities such as microfinance, competitiveness and the HIPC Initiative. Following in importance are cultural and community development, sustainable development and the support for SMEs, which includes CAF's participation in venture capital funds. Other significant portions of these resources are aimed at special programs of the Corporation, such as the IIRSA Initiative and the Governance Program.

Graph Nº 8

**Allocation of funds for technical cooperation and other grant operations***



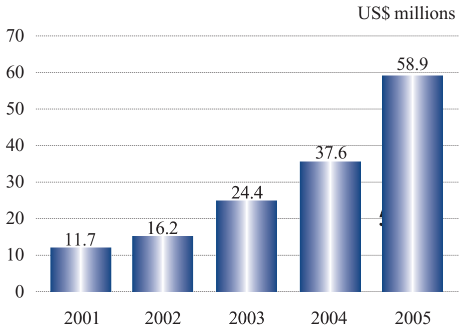

* Includes operations with reimbursable resources from FONDESHU and FIDE

## 5. Microfinance operations

CAF provides support to micro enterprises by strengthening and consolidating financial institutions that channel resources to this sector ( *pp. 103-104*). During 2005, CAF's operations covered 11 countries and 35 microfinance institutions in Latin America. Thus, CAF is among the major multilateral institutions involved in microfinance operations in the region, as shown in *Graphs N° 9*, *N° 10* and *N° 11*.

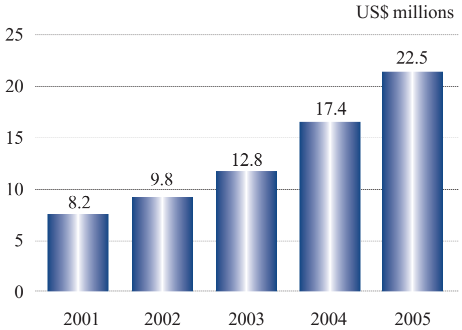
Graph Nº 9

**Microfinance: approvals+renewals**



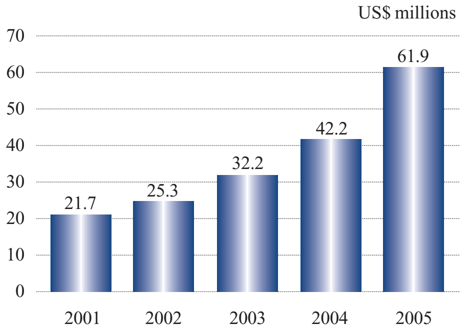

Graph Nº 10

**Microfinance: disbursements**

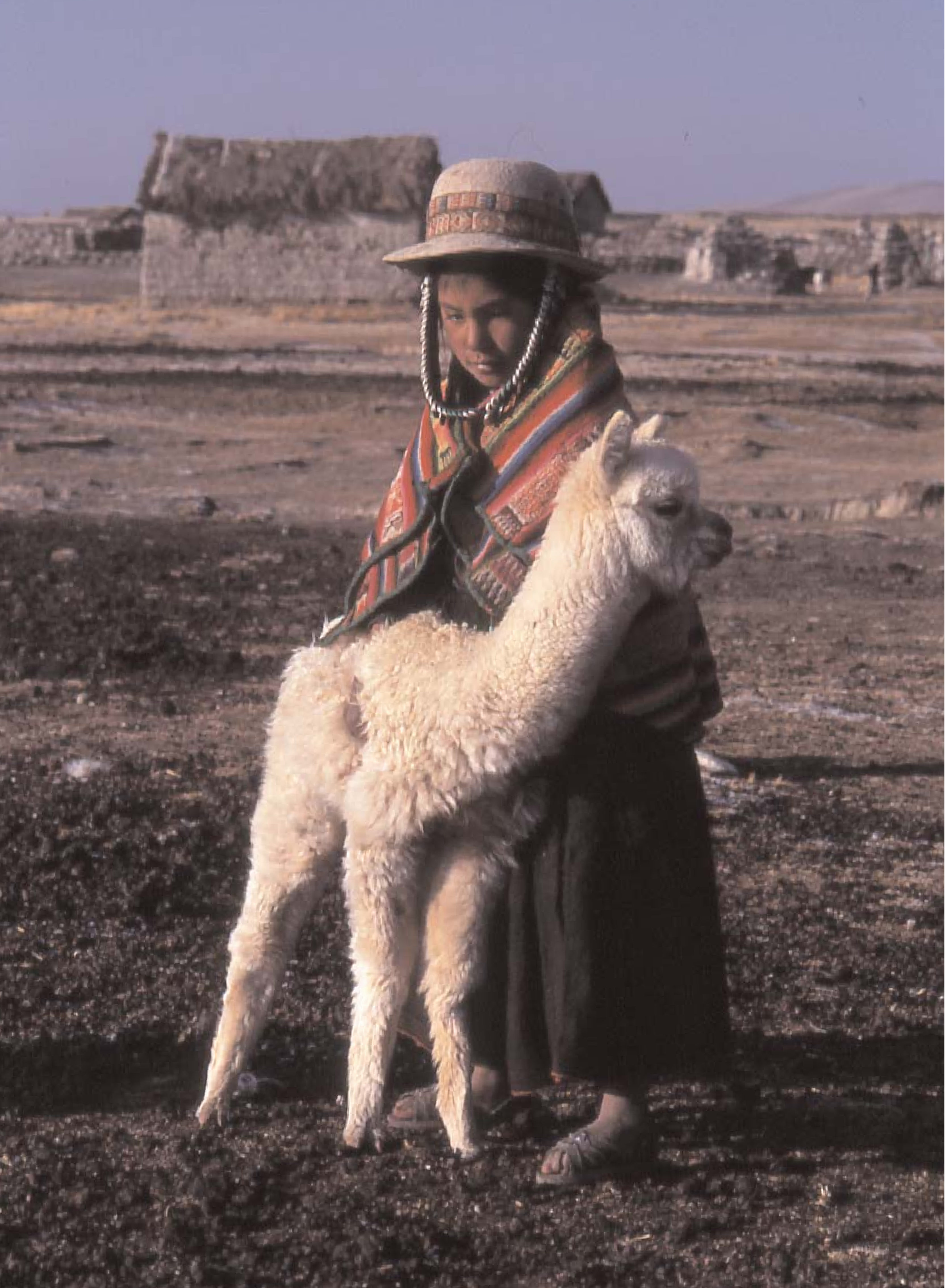



Graph Nº 11

**Microfinance: total portfolio***




* Includes loan and capital investment portfolios, and bond issue guarantees



# Bolivia

***During the past five years (2001-2005) CAF approved US$ 2,608 million in operations for Bolivia –resulting in an average of US$ 522 million per year, equivalent to 14% of the total approvals for the period– while disbursements reached US$ 1,520 million, representing 14% of the Corporation's total disbursements.***

TOTAL APPROVALS for Bolivia in 2005 amounted to US$ 523 million, representing 11% of CAF's total for the year, while disbursements reached US$ 280 million (12% of the total). By year-end, Bolivia's total portfolio* reached US$ 1,125 million, equivalent to 14% of the total.

Sovereign risk loans represented US$ 371 million of total approvals and included infrastructure projects in transportation and energy sectors, with the purpose of increasing productivity and competitiveness in the country.

More specifically, Bolivia's requirements in the critical area of *transportation infrastructure*, were attended by allocating US$ 289 million to improve roads connecting various departmental capitals, to foster international integration with neighboring countries and, in general, to strengthen the transportation sector, in line with the development goals of the IIRSA Initiative. The financing granted to this sector aims to improve the country's competitive profile, by providing agricultural producers with lower transportation costs, while incorporating a large share of the population in the development process. These resources also promote improvements in the living standards of the areas' inhabitants, as they tend to create jobs for both skilled and unskilled workers, and have a strong multiplying effect on other productive sectors. The improvement of the transportation infrastructure also contributes to alleviate the isolation of provinces, municipalities and communities located within the areas of influence of the projects, the connection with Brazil through the road segment Roboré-El Carmen-Arroyo Concepción is of particular significance.

Within the same *economic infrastructure* sector, an additional US$ 32 million were approved to expand the supply of electricity with a 115 Kv transmission line –approximately 374 km long– that will improve the reliability of power supply, reduce emissions from the use of liquid fuels, and generate fiscal savings by reducing the subsidy for the diesel used for power generation.

In the area of *competitiveness, productive sectors and SMEs and Microfinance*, US$ 78 million were approved to foster private investment initiatives, in manufacturing, mining, the dairy products industry and non-traditional exports.

Approvals related to *financial systems and capital markets* totaled US$ 120 million which were channeled to small- and medium-sized enterprises through intermediary institutions, to finance foreign trade and working capital loans.

## Other contributions to Bolivia's sustainable development

Using technical cooperation resources, CAF approved approximately US$ 4 million in grants to meet priorities in both the public and the private sectors; the resources were allocated from the Technical Assistance Fund, the Human Development Fund, the Spanish Funds for Technical Cooperation and the Special Fund for Bolivia, which specifically targets the Heavily Indebted Poor Countries Initiative (HIPC).

In the area of *governance*, the resources were aimed at: Creation of a Cadastral Registry in the Municipalities; Leadership Project, Consensus Building and Institutional Development; strengthening of the Ministry of Basic Services and Public Works; design of a Fiscal Decentralization Strategy which encompasses three government levels: central, intermediate and municipal; and projects to handle information requests and to implement a website for the General Superintendence of SIRESE. Another program was also implemented to improve the sectoral regulatory system, implement reforms, decentralization, citizens' education and constitutional processes. The following are ongoing programs: Governance and

The Productive chaining is giving a boost to the production chain of camelids in Bolivia, a major job-generating sector with a network of 400 camelid breeders.

* Includes the cofinanced component of CAF's portfolio and loans supported by CAF's partial credit guarantee program.

**Operations approved for Bolivia. Year 2005** In US$ millions

| Client and Executing Agency | Operation | Purpose | Amount | Term years | Project Cost |
|---|---|---|---|---|---|
| Republic of Bolivia / Ministry of Public Works and Services | Electric Transmission Line Caranavi-Trinidad | Finance the construction of a 115- Kv electric transmission line, approximately 374 Km long to improve power supply in the country. | 32 | 15 | 47 |
| Republic of Bolivia / National Roads Service (SNC) | Second Transport Sector Support Program (PAST II) | Promote actions to foster physical border integration between Bolivia and its neighboring countries, which serves as a basis for mutual economic development. | 25 | 15 | 41 |
| Republic of Bolivia / National Roads Service (SNC) | Santa Cruz-Puerto Suárez Road Corridor | Improve the operational conditions of the road currently connecting the border city of Puerto Suárez with the city of Santa Cruz, which allows for integration with Brazil, to the East and with Peru and Chile, to the west. | 180 | 15 | 465 |
| Republic of Bolivia / National Roads Service (SNC) | Third Transport Sector Support Program (PAST III) | Promote actions to foster physical integration between Bolivia and its neighboring countries, which serves as a basis for mutual economic development. | 84 | 15 | 131 |
| Minera San Cristóbal S.A. | Corporate Loan | Partially finance the Minera San Cristóbal Project. | 50 | 7 | 681 |
| Various clients | Financing for Trade and Working Capital | Finance foreign trade operations, working capital and investments in capital goods. | 147 | | |
| Various clients | Operations with Technical Cooperation Resources | Various | 4 | Various | n.a. |
| **Total** | | | **523** | | **1,365** |

Political Management, Phase V, with Universidad del Valle and George Washington University; Leadership for Transformation, Phase II, with the IDEA Foundation; and Efficient and Transparent Municipalities (MuNet), Phase II, with the OAS and the Canadian International Development Agency (CIDA).

CAF supported important *competitiveness* projects aimed at promoting entrepreneurial capacity and creation of new enterprises in Bolivia. For the second year in a row, support was given to training workshops for participants in the contest on “Entrepreneurial Ideas 2005”. Support is also being provided to the project “Seeding your Enterprise”, led by the Neo-Enterprise Foundation, whose purpose is to establish the first business incubator in the Department of La Paz. Additionally, the “National Support System for University Enterprises – *Bolivia Emprende*” aims to promote the creation of entrepreneurial centers in the country’s private and public universities, and the project “Costo Bolivia” aims at improving competitiveness by creating indicators to monitor progress in investment climate and other technical aspects that facilitate the conduct of business in the country.

CAF supported a number of projects in *cultural and community development*, aimed at generating capacity and promoting social capital and responsibility, such as the musical education program that supports orchestras, choruses and lutherie activities, as well as the sports training programs in Santa Cruz, La Chiquitanía, El Chaco and El Alto. In the area of productive community management, important achievements were made, particularly as regards community tourism, with support from the authorities of Uyuni, Viacha, Tiwanaku and Southern Titicaca Lake, as well as in the communities of Calamarca and Morochata with two projects aimed at satisfying the population's demand for basic public services –particularly health (concluded) and education. These projects serve to train the population on issues relating to such services with an intercultural and gender-oriented approach.

*Below:*
In the Calamarca and Morochata Municipalities, CAF promotes training for Aymara and Quechua women in order to reduce the high rates of maternal and infant mortality and to vindicate their right to a healthy and decent life.

*Beside:*
The 600 km-long Integration Corridor from Santa Cruz to Puerto Suárez will complete the first asphalt road connection between Bolivia and Brazil, thus promoting national and regional development.

*Right:*
As part of its strategy to support the private sector, CAF has granted financing to Tahuamanu, an enterprise devoted to processing chestnuts for export which has become the main source of employment in the city of Cobija (Pando).

# Colombia

***During the past five years (2001-2005) CAF US$ 4,344 million in operations for Colombia –resulting in an average of US$ 869 million per year, equivalent to 24% of the total approvals for the period– while disbursements reached US$ 2,630 million, representing 24% of the Corporation's total disbursements.***

TOTAL APPROVALS for Colombia amounted to US$ 1,237 million in 2005, representing 26% of CAF's total for the year, while disbursements reached US$ 688 million (29% of the total). By year-end, Colombia's total portfolio* reached US$ 1,985 million, equivalent to 25% of the total.

US$ 783 million of total approvals were sovereign risk operations, with particular emphasis on mass transportation, road and energy infrastructure.

Priority was also given to reforms in the commercial, logistics and pension funds sectors as a mean to contribute to macroeconomic stability, productivity and the competitiveness of the economy. Likewise, non-sovereign loan approvals amounted to US$ 454 million, and were destined to the petrochemical industry, financial system, non-traditional exports and the energy sector.

*Economic infrastructure* loans represented 18% of total approvals (US$ 300 million), with emphasis on road maintenance and construction projects, as well as the energy sector. Thus, US$ 150 million were destined to improve the country's road infrastructure and the sustainability of the national road system, and another US$ 150 million were assigned to the construction of new power transmission lines (500 kv) to reinforce the National grid.

*Social development* loan approvals amounted to US$ 83 million and aim to improve living standards, with emphasis on increasing social equity and facilitating access to public goods and services, such as health services, education and water supply. Of particular importance is the support provided by CAF to Colombia, in increasing the quality and coverage of the country's vaccination system and improving the education system –initiatives that will contribute to increase the well-being and productivity of its human capital.

*Macroeconomic stability and structural reform* loans were approved in support of the country's strategy for economic growth. Thus, US$ 700 million were targeted to strengthening the country's competitive insertion into the global economy and to reduce the fiscal burden resulting from a new round of reforms to the pension system. In the first case, CAF helped to identify reforms needed in several sectors to strengthen the economy's competitiveness and increase the benefits of the country's international insertion. As regards the administration of pension funds, CAF approved a loan to support new reforms that entered into effect with the Legislative Act of July 2005, which will reduce fiscal pressures while improving equity in the coverage of the system.

As for *competitiveness, productive sectors and SMEs and microfinance*, US$ 150 million were approved for the Colombian private sector, to finance investment projects, working capital and commercial credit lines. In the first case, US$ 15 million in corporate loans were approved to support investments in capital goods and productive capacity. Also, US$ 135 million were approved to support small- and medium-sized enterprises through the financial system.

## Other contributions to Colombia's sustainable development

CAF approved approximately US$ 4 million in technical cooperation grants during 2005 for initiatives in the areas of governance, competitiveness, integration, community development and culture.

*Governance* projects aimed at promoting transparency and efficiency in public management and improving financial administration in diverse municipalities. Ongoing programs in 2005 included the Governance and Political Management Program –which is implemented jointly with several universities– and the Leaders for Transformation Program –which is Higher School of Public Administration (ESAP).

*Puente Hormiguero, in Valle del Cauca.* Within the framework of the programs "Roads for Peace" and "Plan 2,500 km", CAF has contributed to improve the quality of the national road network, and to increase the levels of social participation and competitiveness of the national economy.

* Includes the cofinanced component of CAF's portfolio and loans supported by CAF's partial credit guarantee program.

**Operations approved for Colombia. Year 2005** — In US$ millions

| Client and Executing Agency | Operation | Purpose | Amount | Term years | Project Cost |
|---|---|---|---|---|---|
| Republic of Colombia /Ministry of Finance and Public Credit | Pension Funds Constitutional Reform Consolidation Program | Support the government's efforts in the execution of an agenda of multiple actions related to the second round of reforms to pension funds. | 300 | 12,5 | n.a. |
| Republic of Colombia /Ministry of Finance and Public Credit | Partial Credit Guarantee | Support the government's strategy of public debt management. | 150 | 10 | n.a. |
| Republic of Colombia /Ministry Finance and Public Credit | Competitive International Insertion Reform Program | Contribute to improve the nation's competitive profile to potentiate the possible benefits derived from the subscription of free trade agreements. | 250 | 12.5 | n.a. |
| Republic of Colombia / National Roads Institute | Program of Road Infrastructure for Regional Development | Improve the infrastructure of the national road network to foster physical connections within the territory and to increase the sustainability of the national road system. | 150 | 12 | 1,249 |
| Republic of Colombia /Ministry of National Education | Strengthening of Tecnical and Technological Education | Promote the creation of strategic alliances to support the process to strengthen technical and technological education to improve the coverage and internal efficiency of education institutions. | 15 | 10 | 35 |
| Departamento del Cesar | Potable Water and Basic Sanitation Program | Improve the quality and efficiency of water supply and basic sanitation services in Departamento del Cesar. | 42,5 | 12 | 101 |
| Republic of Colombia /Ministry of Social Protection | Strengthening of the Enhanced Inmunization Program (PAI) 2005-2008 | Contribute to increase the population's access to vaccination services for the period 2005-2008. | 25 | 12 | 134 |
| Various clients | Corporate loans and credit lines | Finance foreign trade operations, working capital and investments in capital goods. | 300 | Various | n.a. |
| Various clients | Operations with Technical Cooperation Resources | Various | 4 | Various | n.a. |
| **Total** | | | **1,237** | | **1,518** |

*Competitiveness* resources were also approved to support the conclusion of two strategic projects: "Entrepreneurial modernization of overland cargo transportation in Colombia", in which more than 100 private and official organizations took part; and "Exporte.org", which served to promote 24 Colombian technology-based enterprises in the markets of Chile, Peru and Ecuador. Additionally, CAF's Competitiveness Program started three new projects in Colombia, related to improving the efficiency, productivity and logistics of the "palm oil cluster", the "Cosmetics and Cleansing Products Cluster" and the "Petrochemical and related products cluster", and also promoted a series of fora dealing with issues relating to productivity and social capital in business activities.

In the area of *cultural and community development*, the Corporation continued to support capacity-building projects that also promote social capital and responsibility. As part of the Musical Program that support orchestras, choruses and lutherie activities, Cultural School project was launched in Medellín for the production of musical instrument in alliance with the public sector, businesses and civil society.

The Corporation also continued its sports training projects in excluded communities, such as Ciudad Bolívar in Bogota, the Agua Blanca district of Cali, the Northeastern Commune of Medellín and the Wayúu indigenous community in La Guajira, in alliance with the municipal private and public sectors of these communities. The cocoa family farming project in Valle del Cauca started a new phase and made significant progress in productive community management in a joint effort with local governments, producers, merchants and international participants.

The Andean Children and Youth Choir is the result of the Musical Training Program, through which CAF is promoting citizenship awareness and values as fundamental factors for social and regional integration.

*Right:*
In support to SMEs, CAF conducted an operation to consolidate the National Guarantee Fund of Colombia, which will facilitate access to financing for approximately 5,600 small and medium-sized enterprises.

*Above:*
Boosting exports and competitiveness: The construction of the 8.6 km-long La Línea Tunnel, in the Road Corridor Bogotá-Buenaventura, is aimed at generating substantial savings in terms of travel time and costs between the capital city and the country's main port on the Pacific Ocean coast.

# Ecuador

***During the past five years (2001-2005) CAF approved US$ 2,355 million in operations for Ecuador –resulting in an average of US$ 471 million per year, equivalent to 13% of the total approvals for the period –while disbursements reached US$ 1,590 million, representing 15% of the Corporation's total disbursements.***

TOTAL APPROVALS for Ecuador amounted to US$ 815 million in 2005, representing 17% of CAF's total for the year, while disbursements reached US$ 340 million (15% of the total). By year-end, Ecuador's total portfolio* stood at US$ 1,231 million, equivalent to 15% of the total.

Sovereign risk operations represented US$ 559 million of total approvals, and emphasized investments in mass transportation and road infrastructure, as well as power supply services, with a view to improving productivity and competitiveness. Non-sovereign risk approvals amounting to US$ 256 million were earmarked for corporate projects, microfinancial entities and credit lines for banking institutions, which on-lend these resources towards small- and medium-sized enterprises.

It is important to note that 44% of approvals (US$ 357 million) were destined to *economic infrastructure*, especially for maintenance and improvement of transportation infrastructure, roads and the energy sector. Thus, US$ 107 million were earmarked to improve urban transportation in several cities, which will reduce mobilization time and costs to commuters and improve the efficiency of the system.

In the area of *energy infrastructure*, the Ecuadorian Government received a loan of US$ 250 million to increase the efficiency, financial sustainability and competitiveness of power supply companies in various regions of the country. This program supports reforms in the power sector with the purpose of expanding the generation capacity at lower costs, and financially strengthening energy distribution companies. Measures have also been adopted to attract new investments in this sector, so as to meet the growing internal demand. Such measures include stabilizing financial obligations between power distribution and generation companies, and the reduction of technical losses to lower overall energy costs. This will increase the reliability of the electricity system and gradually reduce costs, thus promoting competitiveness and economic development.

CAF allocated resources totaling US$ 202 million for various projects aimed at key *social development* programs, and to human development and poverty reduction projects. Those resources are intended to develop the social agenda in Ecuador in order to achieve the Millennium Goals, while seeking to boost the efficiency of these programs so as to ensure their effectiveness and a more equitable social investment. A large portion of these resources will be used to expand the coverage, improve the quality and achieve sustainability in the provision of water supply and sanitation services in various communities of the country. In addition, irrigation systems will be developed for the benefit of small farmers and flower growers. Similarly, resources were approved to improve the quality of basic education centers located in rural areas.

In the area of *competitiveness, productive sectors and SMEs and Microfinance*, the Corporation approved operations amounting to US$ 170 million for investment projects, working capital and commercial credit lines, including through corporate loans to various business groups and resources for regulated microfinancial institutions.

In addition, in the area of *financial systems and capital markets*, credit lines amounting to US$ 85 million were approved for operations through financial institutions, primarily destined to small- and medium-sized enterprises.

CAF has supported several projects which are contributing to the urban organization and modernization of Guayaquil, as in the case of the tunnels of Cerro Santa Ana –a natural barrier which divided the city in two in the past– and the renovation of the neighborhood located in Santa Ana to turn into a picturesque urbanization that is now a popular tourist attraction.

## Other contributions to Ecuador's sustainable development

CAF approved approximately US$ 2 million in technical cooperation grants in 2005 from the Technical Assistance and Human Development Funds, and CAF's Special Fund for Ecuador, which were mainly devoted to *competitiveness, governance, and social and community development* programs.

* Includes the cofinanced component of CAF's portfolio and loans supported by CAF's partial credit guarantee program.

**Operations approved for Ecuador. Year 2005** — **In US$ millions**

| Client and Executing Agency | Operation | Purpose | Amount | Term years | Project Cost |
|---|---|---|---|---|---|
| Republic of Ecuador / Ministry of Education and Culture | 21st Century Education | Improve the quality of education services in various basic education centers in rural areas. | 40 | 12 | 57 |
| Republic of Ecuador / Ministry of Energy and Mines | Sector Program for Power Supply System Strengthening | Enhancement of power generation capacity at lower costs and financial strengthening of energy distribution companies. | 250 | 12 | 357 |
| Republic of Ecuador / Ministry of Economy and Finance | Program for Social Investment Insurance -PRAISE- | Support the government in developing Ecuador's social agenda, with special emphasis on social investment. | 100 | 12 | n.a. |
| Cuenca Municipality | Road and Urban Development Program of the Cuenca Municipality | Improve the coverage of the road system in the city of Cuenca. | 42 | 10 | 63 |
| Quito Sewer System and Potable Water Metropolitan Company | Quito Potable Water and Sanitation Program | Improve the quality and coverage of the water supply and sewer systems in the city of Quito. | 25 | 10 | 36 |
| Municipality of the Metropolitan District of Quito/Public Works Metropolitan Company | II Road Program of the Municipality of the Metropolitan Distric of Quito | Optimize the connectivity of the urban transportation system through the construction of a north-south interconnection road in the city of Quito. | 41 | 10 | 61 |
| Provincial Council of Guayas | Guayaquil-Salinas Road Complementary Works Project | Improve traffic conditions in the Guayaquil-Salinas road, with the ensuing social and economic benefits for the population. | 24 | 10 | 97 |
| Republic of Ecuador / Portoviejo Municipality | Portoviejo Potable Water Project | Contribute to improve the coverage conditions, quality and efficiency of potable water supply services in the city of Portoviejo. | 25 | 10 | 36 |
| Republic of Ecuador / Provincial Council of Pichincha | Cayambe-Tabacundo Irrigation System (first phase) | Install irrigation systems in 3,100 hectares of new farming lands and replace the network of secondary and tertiary channels in 1,180 hectares. | 12 | 10 | 16 |
| Various clients | Corporate loans and credit lines | Finance foreign trade operations, working capital and investments in capital goods. | 255 | Various | |
| Various clients | Operations with technical Cooperation Resources | Various | 2 | Various | n.a. |
| **Total** | | | **815** | | **751** |

In the area of *governance*, the resources supported the Regional Meeting of Attorney Generals on issues such as Integration and Judicial Security, the continuation of the Governance and Political Management Program, jointly undertaken by the Pontifical Catholic University of Ecuador and the Catholic University of Guayaquil, and of the Efficient and Transparent Municipalities Program (MuNet).

In the area of *competitiveness*, three projects aimed at strengthening clusters were started. A shoes and leather goods project in the provinces of Azuay is aimed at strengthening productive and commercial capacities of SMEs in this sector, to improve their access to international markets. Two other projects aim

CAF plays an important role in strengthening microfinance institutions in Latin America. Banco ProCredit –which serves approximately 30,000 micro-entrepreneurs– is included in CAF's portfolio of clients in Ecuador.


to improve productivity and strengthen social capital in the automotive bodywork industry in the province of Tungurahua and the timber sector in Pichincha by instilling a productivity culture and capacity-building within the participants in the clusters.

In the area of *cultural and community development*, CAF continued to support initiatives to strengthen capacities and social capital and responsibility. The continued strengthening of the musical program for instrumental and vocal activities which incorporated a number of children and teachers from the area of Solanda, in the outskirts of Quito. This activity was undertaken jointly with "Fe y Alegría". Similarly, CAF began the second phase of the sports training program –in association with Banco Solidario– thereby expanding its coverage to six sports schools in various regions of the country. In the area of productive management and public services, the second phase of the Randimpak project was launched in collaboration with the Ecuadorian Canadian Fund and FUNDAMYF; also, an alliance with REPSOL YPF Ecuador was established to co-finance three projects: *Casa Campesina* in Cayambe, the Populorum Progressio, in the canton of Pedro Carbo, and the Housing Corporation of the Home of Christ –all of which promote micro-enterprise management, community organization and access to credits for poor families.

Several clients in the private sector received financing from CAF this year. For instance, resources were earmarked for enterprises of the Pronaca Group (left), which is a leader in the food sector in Ecuador, and for Nobis Group (right), which supported a project for electricity generation from the combustion of the bagasse from the processing of sugar cane at the Valdez sugar refinery.

*Above:*
Eight-hundred families of indigenous and peasant communities in the canton of Cayambe are benefiting from CAF's support to strengthening organizational and technical capacities in agricultural and commercial activities.

# Peru

*During the past five years (2001-2005) CAF approved US$ 2,801 million in operations for Peru –resulting in an average of US$ 560 million per year, equivalent to 16% of the total approvals for the period– while disbursements reached US$ 2,096 million, representing 19% of the Corporation's total disbursements.*

Total approvals for Peru amounted to US$ 417 million in 2005, representing 9% of CAF's total for the year, while disbursements reached US$ 256 million (11% of the total). By year-end, Peru's total portfolio* reached US$ 1,724 million, equivalent to 21% of the total.

Sovereign risk operations represented US$ 293 million, with particular emphasis to road infrastructure, in order to contribute to productivity and competitiveness in the country. Non-sovereign risk approvals amounted to US$ 123 million and were mostly destined to the financial sector and micro-enterprises.

70% of the total approvals was assigned to *economic infrastructure* projects, especially for maintenance and improvement of road infrastructure, with a view to attaining higher levels of national and regional integration, and promoting regional development by interconnecting vast territories and promoting economic activities that will boost progress in those areas.

In this regard, it should be noted that Peru is pioneering initiatives to encourage the private sector's participation in the construction of public works, to help consolidate development infrastructure. This is the case of two important operations totaling US$ 260 million which were undertaken within the framework of the Initiative for the Integration of the Regional Infrastructure of South America (IIRSA): the construction of the first stage of the Southern Peru-Brazil Interoceanic Corridor, and the Northern Amazonas Corridor. Both of these regions in Southern and Northern Peru offer important opportunities for economic and social development, given the complementarities of their coastal, mountainous and Amazonian sub-regions. The construction of these corridors will have a very positive impact both at the local, national and international levels, given the improvement in passenger and cargo transportation services, the integration of isolated regions for sustainable development of agriculture and cattle breeding, and the development of a physical link between the Pacific and Atlantic Oceans, thus contributing to South American union.

In the area of *competitiveness, productive sectors and SMEs and Microfinance*, the Corporation approved resources for Peru's private sector, either in the form of direct loans or through the financial sector. In this regard, US$ 103 million in credit lines were approved for diverse banking institutions to finance investment projects, working capital and trade lines, mainly for SMEs and Microfinance. Similarly, corporate loans amounting to US$ 5 million were earmarked to support financing of investments in capital goods in the country's private sector.

## Other contributions to Peru's sustainable development

Technical cooperation resources from the Technical Assistance Fund, the Human Development Fund and the Spanish Cooperation Fund, were used to approve US$ 3 million in grants during 2005. The operations attended requirements both in the public and the private sectors, and included programs in the areas of *competitiveness, governance, community development and culture*.

With the purpose of strengthening governance, CAF launched the Leadership for Transformation Program in alliance with Universidad San Martín de Porres and other institutions, with the objective of training leaders in civic-democratic values. CAF also continued with the Governance and Political Management Program, jointly with the Pontifical Catholic University of Peru (PUCP) and the George Washington University, as well as the Efficient and Transparent Municipalities Program in issues of electronic government and cadastre, in alliance with the Organization of American States (OAS) and the Canadian International Development Agency (CIDA).

Channeling resources towards the private sector is fundamental in CAF's strategies for supporting economic development in its shareholder countries. Within this context, financing was granted to QUIMPAC, a major producer of salt, caustic soda and paper in Peru.

* Includes the cofinanced component of CAF's portfolio and loans supported by CAF's partial credit guarantee program.

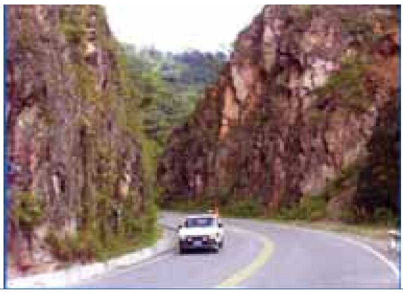
**Operations approved for Peru. Year 2005** — In US$ millions

| Client and Executing Agency | Operation | Purpose | Amount | Term years | Project Cost |
|---|---|---|---|---|---|
| Republic of Peru / Ministry of Finance and Economy | Sovereign Credit Parcial Guarantee | Partially finance the construction of works that form part of a project granted by the government in the sectors of electricity and water supply in the departaments of Cajamarca and Lambayeque. | 28 | 19 | 243 |
| Republic of Peru / Ministry of Transport and Comunications | Program for Studies on Preinvestment for the Border Region with Ecuador | Support the efforts for the development of communities located in Peru's border with Ecuador. | 5,3 | 8 | 9 |
| Concessionary IIRSA Norte S.A. | Northern Amazonas Road Corridor Project | Finance the construction of roads between Paita and Yurimaguas, in order to support integration with neighboring countries and the development of nearby areas. | 60 | 5 | 260 |
| Concessionary Interoceánica Sur, S.A. | Southern Interoceanic Road Corridor Project | Finance the construction of roads between Cusco, Puno, Puerto Maldonado and the border with Brazil (Iñapari), in order to support local and regional integration and potentiate its positive efects on the development of related departments. | 200 | 5 | 719 |
| Various clients | Financing for Trade and Working Capital | Finance foreign trade operations, working capital and investments in capital goods. | 121 | Varios | n.a. |
| Various clients | Operations with Technical Cooperation Resources | Various | 3 | Varios | n.a. |
| **Total** | | | **417** | | **1,231** |

Two new initiatives were undertaken in the area of *competitiveness*: a project related to facilitate "Access of Peruvian Citrus products to the United States" and a contest to promote "Innovative projects by producers' associations", as part of a public-private association effort to promote entrepreneurial development. Other activities included the dissemination of information regarding key issues of the competitiveness agenda for the country in anticipation of the upcoming elections through the following events: "II National Forum on Competitiveness", convened by the National Council on Competitiveness; the "Pending Agenda for Development 2006-2011", convened by CONFIEP; and "Consensus for long term public policies", held during the CADE 2005 Annual Conference of Executives.

In addition, CAF provided support to the negotiations of the Free Trade Agreement (FTA) with the United States, by taking part in the coordination meetings of Andean countries and in the negotiation rounds, together with local working groups. Aside from its logistical and technical support, CAF has financed eight national projects aimed at providing support during the negotiation stage and the implementation of measures after signing the FTA.

Support was given to *cultural and community development* projects aimed at capacity-building and strengthening of social capital and responsibility. Specifically, the Musical Education Program which supports orchestras, choruses and lutherie activities gave rise to the first Youth Orchestra of Peru. The Sports Training Program continued in alliance with local private enterprises, in support of a mostly Afro-Peruvian community in Chincha. At the community level, a project to promote local cooperation



and self-management was carried out in the province of Huaura, and another, in the departments of Puno, San Martín y Ucayali, aimed at training 2,500 poor rural women in the areas of production, marketing, access to credits and relations with local governments to help them enter the labor market.

Finally, CAF granted non-reimbursable technical cooperation resources to the Ministry of Economy and Finance for the "Preparation of mortality tables in Peru", to improve the estimates of the obligations for the public pension fund system. This initiative is also supported by the Pension Office and the Banking and Insurance Superintendence.

*Northern Amazonas Corridor*: With a great commercial impact, this innovating scheme for public and private sector partnership involves the construction of a 114 km-long road, as well as its maintenance and operation for a period of 25 years. It forms part of a 960 km-long road project that will connect the ports of Paita (on the Pacific Ocean coast) and Yurimaguas (on the Amazon River Basin).

Afro-Peruvian children in the San Juan Guayabo Football Academy: CAF promotes social inclusion of less favored sectors of the population through the Sports Training Program.

In order to take full advantage of the new commercial conditions offered by Peru's FTA with the United States, CAF supported a project to identify commercial opportunities for Peruvian fresh citrus products in the U.S. market.

# Venezuela

***During the past five years (2001-2005) CAF approved US$ 3,484 million in operations for Venezuela –resulting in an average of US$ 697 million per year, equivalent to 19% of the total approvals for the period– while disbursements reached US$ 1,885 million, representing 17% of the Corporation's total disbursements.***

TOTAL APPROVALS for Venezuela in 2005 amounted to US$ 627 million, representing 13% of CAF's total for the year, while disbursements reached US$ 208 million (9% of the total). By year-end, Venezuela's total portfolio* stood at US$ 1,137 million, equivalent to 14% of the total.

Sovereign risk approvals totaled US$ 126 million and were mainly focused on the development of transportation infrastructure, aimed at increasing productivity and competitiveness in the country. Over US$ 500 million were non-sovereign risk approvals and were principally aimed at sectors such as petrochemicals, technology and telecommunications.

*Economic infrastructure* absorbed 15% of approvals (US$ 97 million) and was mainly dedicated to maintenance and development of road and mass transportation infrastructure in urban areas, to improve living standards of the population in those areas.

In this regard, the Corporation approved US$ 72 million for the Operational Investment Program of Metro de Caracas; this is the third CAF loan in support of this program for a total of US$ 205 million. The purpose of the loan is to rehabilitate, upgrade and replace operating equipment of the Caracas metro in order to update it, and restore the original performance capacities of four specific components: rolling stock items, railroad tracks, electromechanical equipment and telecommunications systems.

Since 1993, CAF has approved a number of credits in support of mass transportation systems in Venezuela, for a total amount of US$ 1,200 million. Among the beneficiaries of these operations are the Metro companies of Caracas, Valencia, Maracaibo and Los Teques, and the Caracas-Tuy Medio railroad.

Similarly, the Bolivarian Republic of Venezuela received financial resources amounting to US$ 29 million for the area of *social and environmental development*, including resources to support environmental protection and to enhance the coverage of water supply and sanitation services in the country. Likewise, a loan was approved to support and train producers and artisans in semi-arid rural zones in Lara and Falcón states, in order to improve the socio-economic conditions and living standards of approximately 32,500 inhabitants of 271 communities. Special attention will be given to the rehabilitation, management and conservation of micro water basins and the preservation of natural resources through the protection of soils and water sources, as well as reforestation activities.

In the area of *competitiveness, productive sectors and SMEs and Microfinance*, resources were approved to support the Venezuelan private sector, including through US$ 190 million in credit lines for investment projects, working capital and foreign trade lines. In addition, US$ 310 million werer approved for the corporate sector to finance capital investments of important private sector groups.

## Other contributions to Venezuela's sustainable development

With technical cooperation resources, CAF approved US$ 1 million in grants during 2005, to support activities in the areas of *governance, competitiveness and social capital*.

In the area of *governance*, financing was granted for the Automation of the Cadastre System of the Sotillo Municipality; the continuation of the Governance and Political Management Program, in alliance with George Washington University and Andrés Bello Catholic University; and the Efficient and Transparent Municipalities Program, in conjunction with the OAS and the Canadian International Development Agency (CIDA). As part of the activities conducted within the framework of this program, the first workshop on electronic governance was held in Caracas with the participation of more than one-hundred international and local guests.

**Building Bridges Project (CAF-Universidad Metropolitana Agreement).** As part of the formation of social capital in Tacarigua de La Laguna (Venezuela), environmental sanitation activities are being conducted for cleaning the lagoon's canals, with the participation of members of the community, university students and staff of Inparques.

* Includes the cofinanced component of CAF's portfolio and loans supported by CAF's partial credit guarantee program.

**Operations approved for Venezuela. Year 2005** — **In US$ millions**

| Client and Executing Agency | Operation | Purpose | Amount | Term years | Project Cost |
|---|---|---|---|---|---|
| Bolivarian Republic of Venezuela C.A. Metro de Caracas | Metro de Caracas Operative Investment Program | Finance activities for maintenance, upgrading and replacement of equipment in the operative lines of the subway system in Caracas. | 72 | 10 | 606 |
| Bolivarian Republic of Venezuela Ministry of Popular Economy | Sustainable Rural Development Project for semiarid zones in Lara and Falcón States (PROSALAFA II) | Sponsor the construction of structures for basic protection of soils and water collection, in order to improve management and preservation of natural resources. | 4 | 10 | 19 |
| Bolivarian Republic of Venezuela National Fund for Urban Transportation | Urban Transport National Program (Phase II) | Support the improvement of urban transportation system in various cities of Venezuela in terms of quality and efficiency, as well as the institutional strengthening of the entities responsible for this sector. | 25 | 8 | 375 |
| Bolivarian Republic of Venezuela Ministry of Environment and Natural Resources | Environmental Management* Sub-program | Finance a series of actions aimed specifically for environmental and social needs. | 25 | 7 | n.a. |
| Various clients | Financing for Trade, Working Capital and Investment | Support foreign trade operations, working capital and investments in capital goods in productive sectors. | 500 | Various | n.a. |
| Various clients | Operations with Technical Cooperation Resources | Various | 1 | Various | n.a. |
| **Total** | | | **627** | | **1,000** |

*From the reallocation of resources approved as part of a loan for the "Program to Rehabilitate and Modernize the Potable and Sanitation Sectors".

In the area of *competitiveness*, CAF promoted a System to Support the Creation of Enterprises in Venezuela, in alliance with Fundación Ideas and with the participation of the following universities: Los Andes (Mérida), Yacambú (Barquisimeto), Rafael Belloso Chacín (Maracaibo), Francisco de Miranda (Coro), Simón Bolívar and Metropolitana (Caracas); as well as McKinsey & Company, the Institute of Graduate Studies in Administration (IESA), and the business incubators of the technological parks of Sartenejas and Mérida. The System coordinates institutions offering consultancy in identifying business opportunities, training potential entrepreneurs, business incubation and access to financing mechanisms, among other services. In addition, the Corporation sponsored several publications, such as the manual on "Social initiative as a Competitive Strategy", jointly with IESA; "Technology in Venezuela: Present and Future", in alliance with Red Venezuela Sí Compite; and the study "Most attractive cities for investment", in collaboration with the National Council for Investment Promotion.

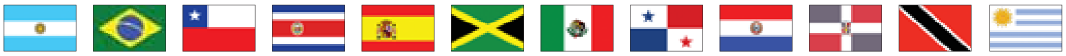
In *community and cultural development*, CAF supported projects for capacity building and strengthening of social capital and responsibility. Continued support was given to the musical education program for orchestras, choruses and lutherie activities. In productive community management, mention must be made of the training program for youngsters in La Guaira through the school-workshop promoted by the Spanish International Cooperation Agency (with which CAF signed an agreement with regional scope) and the Vargas Major's Office. Likewise, the Corporation continued the Paria Project Foundation project, aimed at consolidating capacities for the production and trade of cocoa, organizational capacities regarding health and educational services, and possibilities for community investment and savings. The organization and training of groups in financial self-management (bankomunales), was concluded by Fundefir, and a second phase started, which will consolidate and expand the model for promoting local cooperation, investments and payments through an Internet-based platform for regulations and transfers.

Similarly, the Corporation contributed to several initiatives aimed at issues of significance for the country, such as two grants for the Ministry of Infrastructure for a feasibility study on a Colombia-Venezuela interconnection road –within the framework of the IIRSA Initiative– and studies on mass transportation systems, areas for which CAF has provided substantial support in the last few years.

On its social agenda, CAF has given priority to children and youngsters who receive support through various programs. The picture shows a group of girls working at the School-Workshop in La Guaira, which forms part of a training program in the area of productive community management.

One of the activities conducted to consolidate capacities for cocoa production and trade, within the framework of the project carried out by the Paria Project Foundation with support from CAF.

C.A. Metro de Caracas received new financial support this year –on this occasion to upgrade its operating lines. It should be noted that CAF has been contributing to the development of this mass transportation system for over a decade now in various cities such as Caracas (Line 4, on the left), Los Teques (above), Maracaibo and Valencia.



## Other shareholder countries and multinational operations

DURING THE PERIOD 1996-2005, CAF approved a total of US$ 3,505 million in operations for *Series C* shareholder countries –that is, non-Andean Community countries– while disbursements totaled US$ 2,070 million during the period. At end of 2005, CAF's portfolio* in these countries reached US$ 787 million, representing 10% of the Corporation's total portfolio.

CAF's presence in non-Andean countries strengthened its role as a promoter of Latin American integration as well as its institutional and financial influence in the region. The Corporation's role has also contributed to strengthen its links with these countries and with the other shareholders of the Andean Community. In this regard, it should be noted that during the year the Corporation subscribed shareholder capital increases with the Republic of Argentina (US$ 75 million) and Panama (US$ 10 million), thereby expanding its operational potential in those countries.

CAF also continued to support the Plan Puebla Panama and its interaction with the IIRSA Initiative on a regional basis (*pp. 93-96*). At the same time, CAF strengthened its presence in the most important integration blocs –both at the hemispheric level and in Latin America and the Caribbean– through its active participation in the context of the Andean Community and Mercosur, as well as the summits of the Association of Caribbean States, of the Americas and the Ibero-American Summit, among others (*pp. 21 and 23*).

During 2005, CAF intensified its linkages with *Series C* shareholder countries by undertaking various program missions and visits by its Executive President to countries in South America (Argentina, Brazil, Paraguay and Uruguay), Central America (Costa Rica, Mexico and Panama) and the Caribbean (Dominican Republic). These missions were aimed at identifying and reaching consensuses with the respective governments regarding CAF's medium-term programs in these countries.

Additionally, CAF attained record levels of approvals (US$ 1,127 million), disbursements (US$ 565 million) and portfolio (US$ 787 million) in *Series C* shareholder countries.

Important programs and projects were approved in Argentina, Brazil, Panama, Paraguay and Uruguay, as detailed below.

During 2005, the Executive President of CAF, Enrique García, tightened links with non-Andean shareholder countries. In the first photo García is seen during an official visit to the President of Panama Martín Torrijos, and in the second he appears with Argentina President Néstor Kirchner during the signing of shareholder capital increases agreements between these two countries and CAF. Below, García is with Uruguayan President Tabaré Vázquez.

**Argentina** received an US$ 210 million loan for Concluding the Yacyretá Binational Hydroelectric Complex. This project is a binational (Argentine-Paraguayan) multipurpose investment whose main purpose is to increase electricity generation to supply an additional 7,500 GWh to the interconnected system of both countries, to benefit densely populated areas with substantial industrial production. Additionally, CAF approved a US$ 35 million credit line for the Banco de Inversión y Comercio Exterior (BICE) aimed at financing Argentina's foreign trade with the countries of the Andean Community, as well as a corporate loan to the group Fluviomar Holdings LTD to finance its operation in the Paraguay-Paraná waterway.

CAF approved a total of US$ 695 million for **Brazil**, including US$ 500 million in A/B loans to Eletrobrás (US$ 100 million), and for Votorantim Participações S.A (US$ 400 million), in both cases to support the companies' investment plans. CAF's resources have thereby played a catalytic role as they have attracted financing renowned international financial institutions into Brazil, through the A/B loan mechanism. Likewise, Brazil received substantial resources (US$ 195 million) in credit lines for commercial banks, which were aimed at financing working capital and foreign trade operations of important companies.

CAF approved an US$ 80 million loan to **Panama** to finance the Road Rehabilitation and Improvements Program, with a total investment of US$ 125 million. The project consists in widening the existing road between Arraiján and Chorrera to four lanes and rehabilitating

* Includes the cofinanced component of CAF's portfolio and loans supported by CAF's partial credit guarantee program.

the Tranisthmian Highway between the cities of Panama and Colón. The main objectives of the project are to reduce both vehicle operation costs and travel time, as well as to improve trade and economic activities in the free port zone between Panama City and Colón.

CAF approved an US$ 9,5 million loan for the Republic of **Paraguay**, which will be used to improve and rehabilitate roads that form part of the country's Principal Road Network by financing the Complementary Works Program for National Route 10. The objective is to link important agricultural and cattle railing areas located in the area of influence of Route 10 –in the departments of Canindeyú and San Pedro, Yribu Cuá Municipality– with the country's economic circuit.

*Series C* shareholder countries of CAF have been granted substantial amounts of resources to develop their infrastructure within the framework of regional integration. Such is the case of the Border Center Paso de los Libres/Uruguaiana, shown in the following two photos, the main border crossing in South America (Argentina/Brazil), and the RN81 Corridor (last photo), which is of strategic importance for Brazil' trade with Bolivia, Chile and the markets of the Pacific.


For **Uruguay**, CAF approvals totaled US$ 70 million for the second phase of the Road Infrastructure Program, which aims at improving the conditions of the main national routes and to facilitate not only communications within the country, but also its integration with other Mercosur countries. Part of this approval will take the form of a partial guarantee from CAF, that will mobilize additional resources from capital markets to finance this program –which will definitely generate substantial benefits for domestic and regional trade.

In 2005, CAF also continued to channel resources through disbursements of US$ 33 million for the Integration Corridors in Argentina and US$ 25 million for Eletrobrás in Brazil. Similarly, disbursements to Costa Rica, Uruguay, Panama, Paraguay and Mexico amounted to approximately US$ 13 million for diverse projects and programs in which CAF has an active participation.

As for **Spain**, an agreement was reached for the purchase of nine million tons of $CO^2$ eqv., as part of CAF's efforts to develop markets for the reduction of greenhouse gases through the Latin American Carbon Program (PLAC). In addition, an agreement was formally signed with Caixa de España and the Banco Bolivariano de Ecuador to channel remittances from Ecuadorian emigrants in Spain for the mortgage market in their country of origin, thus ensuring a productive use of their remittances and establishing lasting relations between both institutions.

The Corporation also continued to strengthen relations with various financial agencies in Spain, with which it has undertaken relevant international operations, such as credit lines and A/B loans to finance Spanish trade and investments in the region. Among those institutions are the Institute of Official Credit, Caja Madrid, Banco Bilbao Vizcaya, Banco Santander Central Hispano and Sabadell Atlántico. Moreover, through the Spanish Technical Cooperation Fund, managed by the Corporation, grants are provide for tourism, pre-investment and technical cooperation projects.

As regards Andean and Latin American SMEs, several visits have been made to Spanish institutions such as the Institute of Official Credit (ICO), the Spanish Company for Development Financing (COFIDES) and the Higher Council of Business Chambers, with the purpose of finding areas of common interest with each one of these institutions in order encourage co-financing, internationalization and technical assistance agreements.

## Other contributions to sustainable development and multinational operations

During 2005 CAF approved an approximate amount of US$ 8 million in technical cooperation grants to multinational operations and strategic regional programs for *Series C* shareholder countries; these were financed with resources from CAF's Technical Assistance Funds, the Human Development Fund and the Spanish Technical Cooperation Fund. These funds also financed high priority operations and programs in the areas of integration, competitiveness, governance, environment, community development, culture, microfinance and social development.

## Operations approved. Year 2005

In US$ millions

| Client and Executing Agency | Operation | Purpose | Amount | Term (years) | Project Cost |
|---|---|---|---|---|---|
| **Argentina**<br>Republic of Argentina / Entidad Binacional Yacyretá | "Yacyretá Binational Hydroelectric Complex" Completion Plan | Partially finance an increase in existing electric power supply for Argentina-Paraguay Interconnected systems. | 210 | 15 | 812 |
| Fluviomar Holding LTD | Corporate Loan | Expand cargo transportation capacity in the Paraguay-Parana fluvial system. | 12 | 5.5 | 98 |
| Various clients | Foreign Trade Operations and Working Capital | Finance foreign trade operations and working capital. | 35 | Various | n.a. |
| **Brazil**<br>Votorantim Participações S.A. | Corporate Loan | Finance the company's investment plan, aimed at increasing productive capacity. | 400 | 10 | 400 |
| Centrais Elétricas Brasileiras S.A. Eletrobrás | Investment Plan | Partially finance a plan to invest in assets for power generation and transmission. | 100 | 10 | 100 |
| Various clients | Foreign Trade Operations and Working Capital | Finance foreign trade operations and working capital. | 195 | Various | n.a. |
| **Costa Rica**<br>Banco Improsa | Foreign Trade Operations and Working Capital | Support micro- and small-size enterprises. | 1.5 | Various | n.a. |
| **Mexico**<br>Financiera Compartamos | Foreign Trade Operations and Working Capital | Support micro- and small-size enterprises. | 5 | Various | n.a. |
| **Panama**<br>Republic of Panama / Ministry of Public Works | Road Rehabilitation and Improvement Program | Finance and improvement in infrastructure and security in the National Road Network so as to reduce operation costs and time spent by users on highways. | 80 | 12 | 126 |
| **Paraguay**<br>Republic of Paraguay / Ministry of Public Works and Communications | National Route 10 complementary works Program | Finance the rehabilitation and improvement of existing roads that form part of Paraguay's, Main Road Network, within the context of the Integration Corridors program for the Eastern region. | 9.5 | 10 | 28 |
| Various clients | Foreign Trade Operations and Working Capital | Finance foreign trade operations and working capital. | 1 | Various | n.a. |
| **Uruguay**<br>National Corporation for Development / Corporación Vial del Uruguay | Road InfrastructureProgram, Phase II | Finance the modernization and improvement of the main national routes so as to facilitate integration with Mercosur countries. | 70 | 15 | 295 |
| **Other countries and multinational operations**<br>Various clients | Operations with Technical Cooperation Resources | | 8 | n.a. | n.a. |
| **Total** | | | **1,127** | | **1,858** |

Among these projects are two operations in Argentina: one for improving the regulation of micro-finance institutions and the other for strengthening access to capital markets by a public financial institution to support the expansion of its credit capacity. In addition, resources were granted for the event "Mining in Border Areas: International Cooperation for Sustainable Development" in Brazil, for assistance to the victims of floods in the Caribbean and in Sarapiqui in Costa Rica, for the Meso-American workshop on competitiveness in Mexico, for the IX Meeting of the Meso-American Council for Competitiveness in Panama, and for the Program on Integration Corridors in Western Paraguay, among others.

*Multinational operations*, through which CAF articulates its role as a promoter of Latin American integration, contributed to several important events, including the V Meeting of Former Latin American Presidents, the IX Conference on Trade and Investment in the Americas, the VIII Inter-American Forum on Micro-enterprises, Local Economy and Employment Development in Latin America, Harmonization of National Legislations vis-à-vis Community Rights, Project on Good Practices in Corporate Government, Integral Management and Sustainability of Forests in Tarapacá and Río Algodón (Colombia-Peru), the X International Congress of CLAD on State Reform and Public Administration, the Ibero-American Congress of Ombudsmen, Support to Social Entrepreneurs in Latin America, and the workshop Renewed Agenda on regional and subregional security as a mechanism for prevention of conflicts: A dialogue between the Andean Community and Mercosur.

Finally, it is worth mentioning that CAF has been able to meet common requirements of the countries through its strategic programs with regional scope (*p. 91*), which this year received around 50% of technical assistance resources for developing various fields of action such as: endowment of physical infrastructure, increase in competitiveness, integration of market capitals, bio-trade, prevention and mitigation of damages caused by natural disasters, governance, human and social capital building, and training and updating of journalists and mass media, among others.

In Jujuy, Argentina, part of the Project Network of Rural Tourism in Andean Countries is being conducted in order to consolidate a network of tourist services in peasant and indigenous communities in Argentina, Bolivia and Venezuela.

## Table of approved operations in 2005

US$ Millions

| | Short | Medium | Long | Total CAF |
|---|---|---|---|---|
| **1. Bolivia** | **109.2** | **88.8** | **325.2** | **523.2** |
| Execution of Projects, Programmes and Corporate Loans | | 56.0 | 321.2 | 377.2 |
| International Trade Operations | 109.2 | 32.8 | | 142.0 |
| Technical Cooperation Operations | | | 4.0 | 4.0 |
| Equity Participations | | | | 0.0 |
| **2. Colombia** | **0.0** | **135.0** | **1,101.6** | **1,236.6** |
| Execution of Projects, Programmes and Corporate Loans | | 10.0 | 1,097.3 | 1,107.3 |
| International Trade Operations | | 125.0 | | 125.0 |
| Technical Cooperation Operations | | | 4.3 | 4.3 |
| Participaciones Accionarias | | | | 0.0 |
| **3. Ecuador** | **230.0** | **16.5** | **568.9** | **815.4** |
| Execution of Projects, Programmes and Corporate Loans | 45.0 | 11.0 | 567.0 | 623.0 |
| International Trade Operations | 185.0 | 5.5 | | 190.5 |
| Technical Cooperation Operations | | | 1.9 | 1.9 |
| Equity Participations | | | | 0.0 |
| **4. Peru** | **105.0** | **275.5** | **36.3** | **416.8** |
| Execution of Projects, Programmes and Corporate Loans | 10.0 | 260.0 | 33.3 | 303.3 |
| International Trade Operations | 95.0 | 15.5 | | 110.5 |
| Technical Cooperation Operations | | | 3.0 | 3.0 |
| Equity Participations | | | | 0.0 |
| **5. Venezuela** | **315.0** | **185.0** | **127.1** | **627.1** |
| Execution of Projects, Programmes and Corporate Loans | 275.0 | 35.0 | 125.8 | 435.8 |
| International Trade Operations | 40.0 | 150.0 | | 190.0 |
| Technical Cooperation Operations | | | 1.3 | 1.3 |
| Equity Participations | | | | 0.0 |
| **6. Other Shareholder countries** | **62.5** | **175.0** | **889.8** | **1,127.3** |
| **• Argentina** | **35.0** | **0.0** | **222.4** | **257.4** |
| Execution of Projects, Programmes and Corporate Loans | | | 222.0 | 222.0 |
| International Trade Operations | 35.0 | | | 35.0 |
| Technical Cooperation and FONDESHU operations | | | 0.4 | 0.4 |
| **• Brazil** | **20.0** | **175.0** | **500.0** | **695.0** |
| Execution of Projects, Programmes and Corporate Loans | | | 500.0 | 500.0 |
| International Trade Operations | 20.0 | 175.0 | | 195.0 |
| Technical Cooperation and FONDESHU operations | | | 0.0 | 0.0 |
| **• Costa Rica** | **1.5** | **0.0** | **0.0** | **1.5** |
| Execution of Projects, Programmes and Corporate Loans | | | | 0.0 |
| International Trade Operations | 1,5 | | | 1.5 |
| Technical Cooperation and FONDESHU operations | | | 0.0 | 0.0 |
| **• Mexico** | **5.0** | **0.0** | **0.0** | **5.0** |
| Execution of Projects, Programmes and Corporate Loans | | | | 0.0 |
| International Trade Operations | 5,0 | | | 5.0 |
| Technical Cooperation and FONDESHU operations | | | 0.0 | 0.0 |
| **• Panama** | **0.0** | **0.0** | **80.0** | **80.0** |
| Execution of Projects, Programmes and Corporate Loans | | | 80.0 | 80.0 |
| International Trade Operations | | | | 0.0 |
| Technical Cooperation and Fondeshu operations | | | 0.0 | 0.0 |
| **• Paraguay** | **1.0** | **0.0** | **10.0** | **11.0** |
| Execution of Projects, Programmes and Corporate Loans | | | 9.5 | 9.5 |
| International Trade Operations | 1.0 | | | 1.0 |
| Technical Cooperation and FONDESHU operations | | | 0.5 | 0.5 |
| **• Uruguay** | **0.0** | **0.0** | **70.0** | **70.0** |
| Execution of Projects, Programmes and Corporate Loans | | | 70.0 | 70.0 |
| International Trade Operations | | | | 0.0 |
| Technical Cooperation and FONDESHU operations | | | 0,0 | 0.0 |
| • Other Operations with Cooperation Resources | | | **7.3** | **7.3** |
| **Total CAF** | **821.7** | **875.8** | **3,048.8** | **4,746.3** |
| Execution of Projects, Programmes and Corporate Loans | 330.0 | 372.0 | 3,026.0 | 3,728.0 |
| International Trade Operations | 491.7 | 503.8 | 0.0 | 995.5 |
| Technical Cooperation Operations | 0.0 | 0.0 | 22.8 | 22.8 |
| Equity Participations | 0.0 | 0.0 | 0.0 | 0.0 |
| **Grand Total CAF (In proportion by term)** | **17%** | **18%** | **64%** | **100%** |

# Management's discussion of financial condition

DURING 2005, rating agencies recognized once again CAF's credit quality and franchise value in the region. Moody's Investor Service upgraded CAF's long-term rating to "A1" from "A2", while Standard & Poor's and Fitch Ratings ratified CAF's credit ratings. Also, in October 2005, Japan Credit Rating Agency (JCR) assigned for the first time a "AA-" credit rating for CAF's foreign currency long-term senior debt (*Table N°1*).

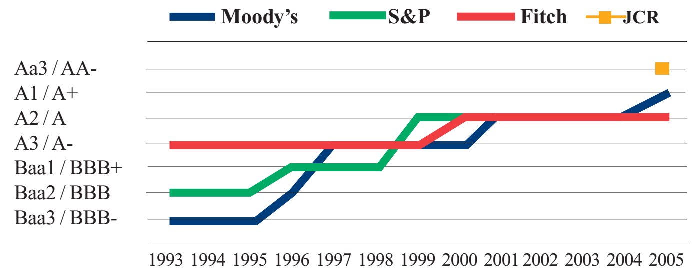
These decisions reaffirm CAF's condition as the best rated frequent issuer in Latin America and are based on the strength and stability of its operating results, its prudent lending policies and political independence, and the continuing support of its shareholder countries.

Table N° 1

**Credit ratings** — December 31, 2005

| | Long-term | Short-term |
|---|---|---|
| Standard & Poor´s | A | A-1 |
| Moody´s | A1 | P-1 |
| Fitch | A | F1 |
| Japan Credit Rating Agency | AA- | - |

**Credit rating evolution**




Moreover, in 2005, CAF was reaffirmed as the most important source of multilateral financing for the Andean region as shown by record levels of approvals and disbursements achieved in that year: US$ 4.7 and US$ 2.3 billion, respectively. It is worth mentioning that 83% of approvals and 79% of disbursements were directed toward medium and long-term project financing.

CAF received US$ 203 million in new capital contributions from its shareholders in 2005. From this total, US$158 million were contributions made from the Andean member countries, which were made as per two simultaneous capital increase programs subscribed by these countries, as well as the completion of committed payments on behalf of the Republics of Argentina, Brazil, Panama and Uruguay. In addition, during 2005 the Republics of Argentina and Panama increased their paid-in capital by subscribing to an additional US$ 75 million and US$ 10 million, respectively.

Net profits also reached a new record in 2005, totaling US$ 283 million, a 36% increase compared to 2004 levels, mainly attributable to the increase in interest rates and a lower allowance for loan losses. The improvement in the economic conditions in the region reflected through the upgrading of some of the countries' credit ratings, as well as the maintenance of a high credit quality loan portfolio, also contributed in the growth of net profits through a lower requirement for loan loss provisions.

Bond issues in the international markets reached US$ 585 million for the year, including a bond in the Samurai market for JPY 20 billion, which was the first issue from a Latin American borrower in that market since July 2001 (*Table N°2*).

Table Nº 2

**2005 Issues in the International Markets**

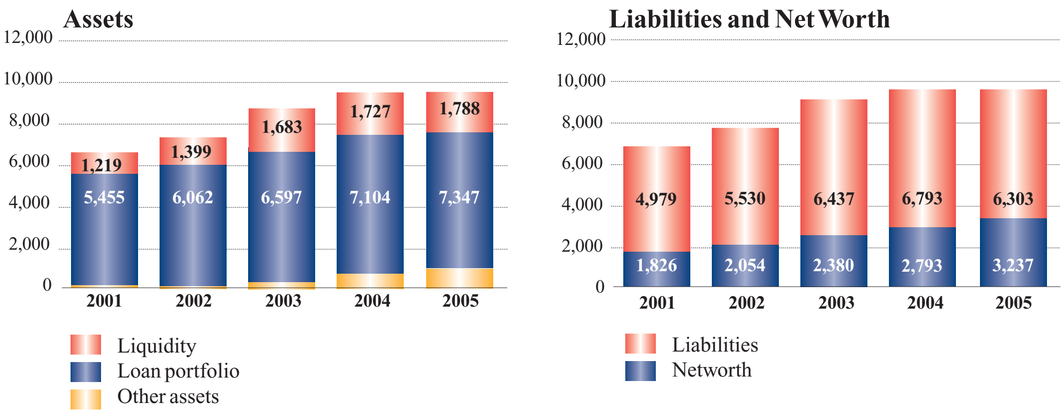
| Date | Market | Amount in original currency of issuance (in million) | Equivalent in US$ million |
|---|---|---|---|
| **Bond Issuance** | | | |
| May | Dollars | US$ 250 | 250 |
| July | Samurai | JPY 20.000 | 185 |
| July | Condor | US$ 150 | 150 |
| | **Sub-total 2005** | | **585** |
| **Short-Term Issuance** | | | |
| **Programs** | Commercial Paper (US) | US$ 1.000 | 1.000 |
| | Commercial Paper (Europe) | US$ 500 | 500 |
| | Short-term Note (Spain) | EUR 500 | 600 |
| | **Sub-total 2005** | | **2,100** |
| | **Total 1993-2005** | | **9,203** |

## Summary of financial statements

During 2005, productive assets –liquidity and loan portfolio– grew at a rate slightly higher than 3%. At December 31 2005, total assets were US$ 9.5 billion, 0.5% lower than at the end of 2004 (*Graph N°1*). This reduction was mostly due to a decrease in the valuation of derivative instruments. Conversely, the loan portfolio amounted to US$ 7.3 billion or 3.5% over the amount at the end of 2004. The other major component of assets, liquidity, totaled US$ 1.8 billion, the equivalent of 19% of total assets and 29% of total borrowings.

Graph N°1

**Balance Sheet** — **As of December 31 of each year (US$ millions)**




Shareholders' equity was US$ 3.2 billion at the end of 2005. New capital payments from shareholders totaled US$ 203 million for the year. In addition, retained earnings reached US$ 283 million.

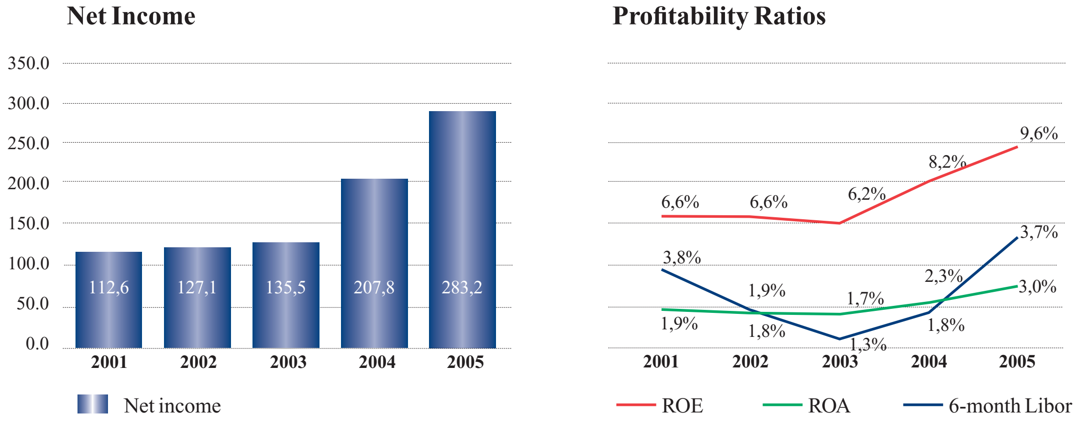
Shareholders' equity represented 34% of total assets and 40.6% of risk-weighted assets, according to Basle Accord standards, as of 31 December 2005.

As mentioned above, net income for the year represented an increase of 36% compared to the previous year, reaching a record level of US$ 283 million. This result was mostly due to several concurrent events, among which was the substantial increase in international interest rates during 2005* , as well as a lower requirement of provisions for loan losses motivated by an improvement in the credit quality of the loan portfolio and the more favorable economic situation currently present in Latin America. This combination of factors produced an increase in net interest margin from 2.6% in 2004 to 3.5% in 2005. Nevertheless, it is worth mentioning that it is unlikely that these events will repeat themselves simultaneously in future years, which would result in more common levels of profitability.

Moreover, the return on equity for the year was 9.6% which compares very favorably with the established benchmark of six-month Libor (*Graph N°2*), while the return on assets for this period was 3%.

Graph N° 2

**Net Income and Profitability** **For the period ended December 31 of each year (US$ millions)**




## Loan portfolio

The loan portfolio was US$ 7.3 billion at the end of 2005 compared to US$ 7.1 billion at the end of 2004, representing a 3% increase.

The distribution of the loan portfolio continued to be skewed toward the financing of public sector projects, which represented 88.8% of the total at the end of the year. From the perspective of distribution by country, the largest exposure was Colombia with 26% of the total loan portfolio, followed by Peru with 23%, Ecuador with 17%, Venezuela with 15%, and Bolivia with 13%. Other non-Andean countries shared 4% of the total loan portfolio. CAF's policies limit exposure to any individual country to a maximum of 30% of the total loan portfolio. Consistent with its objectives, CAF's main activity is the financing of infrastructure projects, which represented 61% of the loan portfolio at the end of 2005.

From the point of view of asset quality, the loan portfolio maintained its excellent credit quality (*Table N°3*). Non-performing loans amounted to US$ 1.3 million or 0.02% of the loan portfolio, while loan-loss provisions totaled US$ 162 million or 2.2% of the loan portfolio. Loan write-offs were US$ 10.4 million for the year.

* Average six month Libor rate increased to 3.70% for 2005 compared to 1.81% for 2004.

Table N° 3

**Asset Quality** — In US$ million

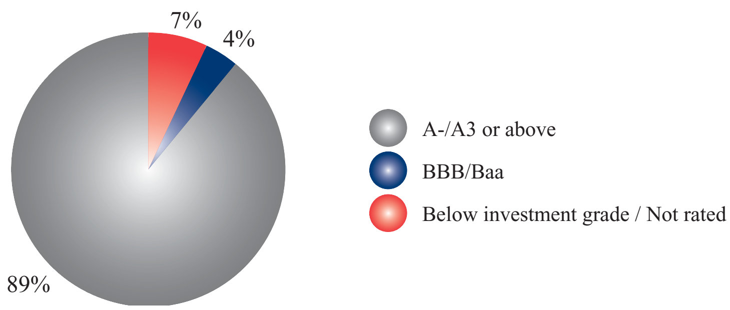
| | 2001 | 2002 | 2003 | 2004 | 2005 |
|---|---|---|---|---|---|
| Overdues | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 |
| Loans in non-accrual status | 33,8 | 29,3 | 10,9 | 20,0 | 1,3 |
| Allowance for loan losses | 177,0 | 196,3 | 209,8 | 181,8 | 161,6 |
| Overdue as a percentage of loan portfolio | 0,00% | 0,00% | 0,00% | 0,00% | 0,00% |
| Non-accrual loans as a percentage of loan portfolio | 0,62% | 0,48% | 0,17% | 0,28% | 0,02% |
| Allowance as a percentage of loan portfolio | 3,24% | 3,24% | 3,18% | 2,56% | 2,20% |

## Liquid investments

At December 31 2005, liquid investments totaled US$ 1.8 billion, which represented 19% of assets and 29% of borrowings. The investment portfolio was characterized by a short duration, an average of 0.32 years, and excellent credit quality (*Graph N°3*): 89% of liquid assets were rated A-/A3 or better, 4% were rated BBB/Baa, and 7% were either not rated or rated below investment grade. CAF's policies require that at least 80% of liquid investments be held in investment-grade instruments and that the average duration be no more than 1.5 years.

Graph N° 3

**Liquid Assets** — As of December 31, 2005



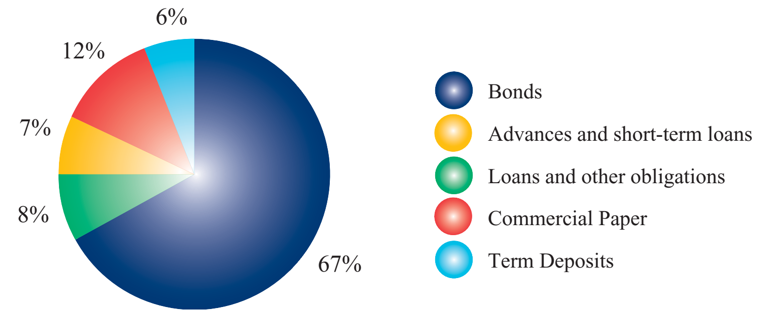

## Funding

During 2005 bond issuance reached an amount of approximately US$ 585 million in several transactions. Among these, it is worth noting the return to the Samurai market, where CAF had not participated since July 2001, with a bond issue for JPY 20 billion. In addition, it is also worth pointing out the second Condor bond issue for US$ 150 million, which is registered in Luxemburg, Peru and Ecuador, and distributed among investors in the region. CAF also maintains an important presence in short-term markets through the continuous use of Commercial Paper Programs in the US and European markets, as well as the Spanish Short-term Note Program.

At December 31 2005, 91% of CAF's funding came from the international capital markets. Bonds represented the main source of with 67% of total funding (*Graph N°4*). In addition, 19% corresponded to commercial paper and short-term loans, 8% to medium and long-term loans and lines of credit, and 3% to deposits from institutions in the Andean region. CAF has long-standing relations with the most important international banks, with official institutions from around the world, and with other multilateral financial institutions.

Graph N° 4

**Liabilities** **As of December 31, 2005**




## Capital

During 2005, CAF received new capital contributions from its shareholders for US$ 203 million. At December 31 2005, shareholders' equity totaled US$ 3.2 billion, a 16% increase compared to the end of 2004. This increase derived from new capital contributions as well as retained earnings. As a result of the increase in shareholders' equity, capitalization ratios continue to be well within CAF's policies on this matter (*Table N°4*). As of the end of 2005, all shareholders were current in their equity obligations to CAF.

Table N° 4

**Capitalization Ratios**

| | 2001 | 2002 | 2003 | 2004 | 2005 |
|---|---|---|---|---|---|
| Gearing (times) [1] | 3,1 | 3,1 | 2,9 | 2,7 | 2,4 |
| Leverage (times) [2] | 2,6 | 2,4 | 2,4 | 2,1 | 1,8 |
| Capital / Risk Weighted Assets (BIS) [3] | 30,8% | 31,3% | 34,3% | 36,5% | 40,6% |

**1** According to internal financial management policies, this exposure measure should be less or equal than 4.0
**2** According to internal financial management policies, this indebtness measure should be less or equal than 3.5
**3** According to internal financial management policies, this level of capitalization should be greater or equal than 30%

## Asset-Liability management

In order to reduce foreign exchange and interest rate risks, CAF's lending and borrowing activities are primarily conducted in floating-rate US$. At December 31 2005, 99.8% of assets and liabilities were denominated in US$ after swaps, and 98.1% of assets and liabilities were based on six-month US$ Libor. Transactions that are not denominated in US$ and based on six-month US$ Libor are swapped into these terms. The swap book totaled US$ 3.6 billion at the end of 2005. CAF's policies require that swap counterparties be rated at least A/A2. CAF does not engage in trading of derivatives and these are used for hedging purposes only.

CAF also seeks to maintain a conservative relationship between the average life of assets and the average life of liabilities. At December 31 2005, the average life of assets was 3.9 years and the average life of liabilities was 4 years.

# CAF: an agenda for integration, growth, competitiveness and sustainable development

## CAF: an agenda for integration, growth, competitiveness and sustainable development

DURING 2005, AN IMPORTANT PART OF CAF'S efforts focused on deepening and consolidating a renewed agenda for Latin America's development. Its main goals are the reduction of poverty and unemployment, the preservation of the region's natural resources, the strengthening of democracy and the involvement of society through the generation of social and human capital. It is the vision of CAF that these goals can be attained through high-rate, top-quality, sustained, equitable and inclusive development in an integral manner.

**CAF has applied all of its experience, knowledge, resources, and action strategies to the execution of its Renewed Agenda for Development in Latin America**

To achieve sustained economic growth is not enough just macroeconomic stability. It also important microeconomic reforms through national debates where different stakeholders interact to find solutions, including businessmen, workers, and representatives of the community, be at the national level or at a small community project. All of these actors matter when designing or promoting development policies.

To achieve these goals, CAF has several operative units and special programs complementing its traditional business management line, providing financial and non-financial services. These programs –mostly established by CAF– have a regional scope and promote strong regional integration. They include sustainable physical infrastructure, competitiveness and support to regional trade, strengthening of the private sector and of micro, small and medium-sized enterprises, generation and dissemination of knowledge regarding development-related issues. These activities are framed under two fundamental principles: the environmental and the social and cultural agendas.

### Renewed agenda for regional development: CAF's strategy

In 2005, CAF's activities for supporting the renewed agenda for regional development were based on the following activities:

***Sustainable physical and logistic integration:***

- IIRSA – Initiative for Regional Infrastructure Integration in South America
- Puebla-Panama Plan

***Competitiveness, productivity and international insertion:***

- PAC – CAF Competitiveness Program
- Kemmerer Program for Development and Integration of Financial Markets and Corporate Governance
- First-Class Ports Program
- Research Program in Development Topics

***Social agenda for an inclusive and equitable human development:***

- Social Investment in Member Countries
- Cultural and Community Development Program
- SMEs and Microfinance
- Governance Program

***Sustainable environmental agenda:***

- PLAC – Latin American Carbon Program
- BioCAF – Biodiversity Program
- Sustainable Development Program in Financial Institutions
- PREANDINO – Andean Program for Disaster Risk Prevention and Mitigation

## Sustainable physical and logistic integration

CAF gives top priority to developing physical infrastructure in South America that articulates land strips with common characteristics across countries, providing support to productivity, competitiveness and social development. Over the last 12 years, CAF's activities have increasingly focused on this business area, which has turned into one of the most important sectors in the Corporation's investment portfolio. In 2005, infrastructure accounted for 37.1% of total loan approvals and 34.8% of disbursements.

During the year, CAF's activities on sustainable physical and logistic integration promoted the following strategic institutional objectives:

- Integration, competitiveness and productivity in the region.
- Equitable and solidary social and human development.
- Institutional development and governance strengthening in the region's countries.
- Responsible and sustainable utilization of natural resources.
- Leverage CAF's financial role in the region.

To achieve these objectives, multiple financial instruments were combined with studies and regional workshops that allowed the exchange of experiences, the strengthening sectoral experts networks, and the analysis of public policies and management of public infrastructure. Complementarily, the Corporation prepared and published Sector Reports on Transportation, Energy and Telecommunications Infrastructure development for each of the Andean countries, with the objective of promoting technical dialogues to design new investment projects and improve sector policies.

In addition, in 2005 CAF played a substantial leadership role in supporting innovative mechanisms to promote private sector participation, allowing governments to develop a larger amount of infrastructure projects, in spite of the limitations due to debt levels and fiscal expenditures. These projects required joint efforts from various areas of the Corporation, which undertook tasks for finding private-

### Development of integration corridors in Peru: An example of a Public-Private Partnership

Based on an initiative of the President of Peru and on the priority placed by all South American countries to regional physical interconnection projects, the Ministry of Transportation and ProInversión implemented an innovative process for private participation in 25-year long concessions for the construction and operation of two major roads to promote integration: the Northern Amazonas Corridor and the Southern Interoceanic Corridor. The private sector is in charge of financing the required investments, executing works, and conducting operative maintenance during the concession, and in return would receive annual payments for 15 years. CAF plays an essential catalytic role in these projects by granting credit lines with repayment terms of 3 to 5 years that can be made readily available to concessionaires, allowing a prompt start of works and facilitate structuring of the required financing to the private sector. The government, therefore, is developing needed national and international integration infrastructure, amounting total investments for nearly one billion U.S. dollars, without increasing the level of public debt. As part of the government's strategy, CAF is supporting an action program for the mitigation of social and environmental impacts in their area of influence. This program, which is being executed in parallel with the construction of the corridors, includes the strengthening of management capabilities for protected natural areas, the preparation of plans for geographical organization, and the creation of the Peru-Bolivia biological corridor.

sector financial solutions to be executed in the long term (15 to 20 years) at reduced costs, while guaranteeing social and environmental sustainability and strengthening of sector managerial capabilities. CAF established a special fund for concessional financing of pre-investment studies, necessary to finance and develop complex projects with a strong impact on regional development.

Every country's significant needs of infrastructure investments, together with existing fiscal limitations to sustain macroeconomic stability, require new mechanisms to finance needed projects. CAF foresees a significant growth in financing loans involving the private sector that will further public sector development objectives.

**IIRSA Initiative during 2005**

Within the framework of the IIRSA Initiative, CAF has financed several projects belonging to the Bolivia-Brazil Integration Corridor –which is of substantial relevance for both regional integration and national road networking, as it will connect the departments of Potosí, Chuquisaca and Tarija in Bolivia.

To South American countries, it is an urgent priority to generate, retain and distribute the largest amount of benefits from production and trade within the region, and to protect their economies from fluctuations in global markets. South American countries are increasingly integrating their economies to gain scales allowing the development of highly competitive productive sectors in global markets and foster constructive and balanced relations with other regions of the world. To accomplish these goals, governments understand that it is imperative the advancement in regional integration.

The construction of a well-articulated, functional and fully-integrated geo-economic space in South America to meet the requirements of productive activities on a regional scale, entails a consistent reduction of internal barriers to trade as well as the development of new infrastructure for transportation, energy supply and telecommunications.

The Initiative for Regional Infrastructure Integration in South America (IIRSA) has received a strong impulse from the highest political levels in the region to sustain regional efforts to physically integrate South America. Launched in late 2000 with the participation of 12 South American countries, this initiative has become the main South American forum to promote the region's process of physical articulation, and counts on the sustained and strong support of CAF and other multilateral financial institutions.

Within the context of the IIRSA Initiative, the regional infrastructure has been organized into ten Development and Integration Hubs (EID, by its Spanish acronym) along business and productive chains capable of large scale economies, either for regional consumption or for export to global markets. Thus, the EIDs represent a territorial reference for the aggregate and sustainable development of South America. This dynamic mechanism seeks to facilitate access to zones with a high productive potential –which are relatively isolated or are being underutilized due to a scarce supply of basic infrastructural services– and to promote mechanisms for a rational and well-balanced distribution of the benefits of development to the territories of the region.

In 2005, South American governments´ activities under IIRSA focused on: (i) the dissemination of information about the strategic approach and on the portfolio of physical integration projects agreed by the working groups on EIDs, and (ii) on the debate of those projects with the private sectors, academic authorities and civil society. Multilateral institutions provided substantial support to the initiative through the financial and technical support of concrete projects being part of the portfolio. It should also be added that CAF led efforts to finance seven new investment projects in infrastructure prioritized by shareholder countries for a total amount of US$ 734,8 million (*p. 94*).

## Puebla-Panama Plan

CAF has supported the Meso-American initiative from its beginnings in 2001, in line with the basic pillars of its institutional mission, namely: promoting sustainable development, Latin American integration and competitiveness. Thus, CAF is contributing to promote social and eco-

**Physical integration projects financed by CAF**

US$ MM

| * | CAF's Contribution | Total Investment |
|---|---|---|
| **Andean Hub** | | |
| 1 Venezuela: Caracas railroad link to the national network | 360.0 | 1,932.0 |
| 2 Venezuela: Support to commercial navigation in the Orinoco – Apure river system | 10.0 | 14.3 |
| 3 Colombia: Buenaventura – Bogota Corridor (La Línea Tunnel) | 32.0 | 278.6 |
| 4 Ecuador: Amazon link to Colombia and Peru (Oriental Main Road) | 93.8 | 152.7 |
| **Guyanese Shield Hub** | | |
| 5 Brazil: Venezuela – Brazil road connection | 86.0 | 168.0 |
| 6 Brazil: Venezuela – Brazil power transmission line | 86.0 | 210.9 |
| 7 Venezuela: Ciudad Guayana – Maturín – Sucre State railroad study | 2.6 | 2.6 |
| 8 Venezuela: Ciudad Guayana (Venezuela) – Georgetown (Guyana) road connection, technical design study | 0.8 | 0.8 |
| **Amazonas Hub** | | |
| 9 Ecuador: Access to the Putumayo River (Julio Andrade – Santa Bárbara – La Bonita road sections) | 7.4 | 10.7 |
| 10 Ecuador: Central Trans-Andean connection (Tandapi – Aloag section) | 26.3 | 43.8 |
| 11 Ecuador: Southern Trans-Andean corridor | 70.0 | 110.2 |
| 12 Peru: North Amazonas Corridor | 110.0 | 328.0 |
| 13 Peru: Ecuador border area infrastructure preinvestment | 5.3 | 8.7 |
| 14 Peru: Central Amazonas Corridor (Tingo María – Aguaytía – Pucallpa section) | 3.5 | 13.6 |
| **Peru-Brazil-Bolivia Hub** | | |
| 15 Brazil: Rondonia State Integration road program | 35.0 | 89.2 |
| 16 Peru: Interoceanico Sur Road Corridor, Sections 2, 3 and 4 | 200.0 | 1,073.5 |
| **Interoceanico Central Hub** | | |
| 17 Peru: Bolivia – Peru integration road corridor | 48.9 | 176.6 |
| 18 Bolivia: Bolivia – Chile integration road corridor | 8.0 | 88.0 |
| 19 Bolivia: Santa Cruz - Puerto Suárez integration road corridor, section 3, 4 and 5 | 280.0 | 465.4 |
| 20 Bolivia: Bolivia – Argentina integration road corridor | 194.0 | 492.0 |
| 21 Bolivia: Bolivia – Paraguay integration road corridor | 60.0 | 182.6 |
| 22 Bolivia / Brazil: Bolivia – Brazil gas pipeline | 215.0 | 2,055.0 |
| 23 Bolivia: Transredes gas pipeline | 88.0 | 262.8 |
| **Mercosur – Chile Hub** | | |
| 24 Argentina / Brazil: Paso de los Libres – Uruguaiana frontier center | 10.0 | 10.0 |
| 25 Argentina: Buenos Aires – Santiago Corridor (Laguna La Picasa roads bypass) | 10.0 | 10.0 |
| 26 Argentina: Buenos Aires – Santiago Corridor (Laguna La Picasa railroad bypass) | 35.0 | 50.0 |
| 27 Argentina: Buenos Aires – Santiago (paso Pehuenche, RN40 and RN 145 access) | 26.7 | 38.1 |
| 28 Argentina: Yacyreta Binational Hidroelectric Complex | 210.0 | 812.0 |
| 29 Uruguay: Megaconcession of the principal roads connecting Argentina and Brazil | 25.0 | 136.5 |
| 30 Uruguay: Road Infrastructure Program, Phase II | 70.0 | 295.4 |
| **Capricornio Hub** | | |
| 31 Argentina: Paving of RN 81 | 16.6 | 16.6 |
| 32 Argentina: Access to Paso de Jama (Argentina – Chile border crossing) | 54.0 | 54.0 |
| 33 Argentina: Study for the Jujuy – La Quiaca railroad | 1.0 | 1.0 |
| 34 Paraguay: Rehabilitation and paving of integration corridors: RN 10 and 11 and complementary works | 19.5 | 41.9 |
| **Paraguay – Paraná Waterway Hub** | | |
| 35 Navigation, institutional and financial operations improvement study of the Waterway (Argentina, Bolivia, Brazil, Paraguay and Uruguay) | 0.9 | 1.1 |
| **Total** | **2,531.3** | **9,161.2** |

* The number of each project indicates its location in the map found on the following page.


Riohacha
P. Fijo
Coro
Pto. Cabello
Maracay
Barcelona
Cumana
Barranquilla
Cartagena
Maracaibo
Cabimas
Caracas
Barquisimeto
Maturin
Trujillo
Tucupita
Calabozo
Panama
San Fernando de Apure
Ciudad Guayana
Merida
Cucuta
San Cristobal
Tumeremo
Georgetown
VENEZUELA
Arauca
Paramaribo
Pto. Carreño
Pto. Páez
Linden
Medellin
GUYANA
Cayenne
Tunja
Manizales
Bogota
SURINAME
Ibague
Villavicencio
GUAYANA FRANCESA
Buenaventura
COLOMBIA
Boa Vista
Lethem
Cali
Popayan
Tumaco
Mocoa
Esmeraldas
La Bonita
Quito
Mapaca
Tena
Belem
Manta
Ambato
ECUADOR
Salinas
Santarem
Altamira
Guayaquil
Cuenca
Manaus
Machala
Iquitos
Itatuba
Fortaleza
Loja
Talara
PERU
Teresina
Paita
Jaen
Olmos
Tarapoto
Natal
Humaita
Sousa
Chiclayo
Cruzeiro do Sul
Campina Grande
Porto Velho
Trujillo
Pucallpa
Recife
Chimbote
Tingo María
Río Branco
BRAZIL
Huaraz
Iñapari
Riberalta
Lima
Aracuajo
Huancayo
Callao
Pto. Maldonado
Ayacucho
Cusco
Feria de Sanana
Cuiaba
Puno
BOLIVIA
Itabuna
Arequipa
La Paz
Brazilia
Desaguadero
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Moquegua
Cochabamba
Gioania
Ilo
Oruro
Sta. Cruz
Arica
Corumba
Sucre
Pto. Suarez
Uberlandia
Pisiga
Potosi
Gral. Eugenio A Garay
Campo Grande
Belo Horizonte
Iquique
Inf. Rivarola
Tupiza
Mcal. Estigarribia
P. J. Caballero
Tarija
Rio de Janeiro
La Quiaca
Yacuiba
PARAGUAY
Concepción
Mejillones
Santos
Antofagasta
San Salvador del Jujuy
Asuncion
Salta
Ciudad del Este
Curitiba
San Miguel de Tucumán
Encarnación
Copiapo
Resistencia
Posadas
Santiago del Estero
Laguna
CHILE
Po. de Los Libres
Caxias do Sul
La Rioja
Uruguaina
La Serena
Porto Alegre
ARGENTINA
Artigas
Cordoba
Rivera
Salto
Pelotas
Villa Maria
Paysandu
Río Grande
Mendoza
Rosario
URUGUAY
Treinta y Tres
Valparaiso
San Luis
San Antonio
Santiago
Mercedes
Colonia
Montevideo
San Rafael
Junin
Buenos Aires
Talca
Sta. Rosa
Concepcion
Mar del Plata
Victoria
Bahia Blanca
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Legend
Existing system of public roads
CAF public roads system project
CAF electrical interconnection project
CAF gas pipeline project
CAF railroad project
Waterways
Hidroelectrical plant
CAF border crossing project
Nation’s capital
Other cities
Ports

**CAF plays a key role in coordinating Latin American integration, by promoting infrastructure projects and favoring sustainable economic and social development, as well as environmental protection**

nomic development in the nine South-South-Eastern Mexico states and the Central American Isthmus countries.

The Corporation provides its support through the Inter-institutional Technical Group (GTI, by its Spanish acronym) created by the Presidents of Central America for the development of programs and projects inserted in the various initiatives of the Plan. Apart from CAF, other regional and international financial institutions are participating in the GTI, such as the Central American Bank for Economic Integration and the Inter-American Development Bank, along with other organizations that provide specialized technical assistance, such as ECLAC, the UNDP, the Central American Institute for Business Administration and the regional entities of the Central American Integration System (SICA).

Similarly, non-reimbursable technical cooperation was granted to CAF member countries belonging to the Plan Puebla-Panama to support strategic planning and pre-investment studies required for those programs and projects under the Plan that can be financed by the Corporation. Also, in 2005, support was given to two important events held by the Meso-American Council on Competitiveness: the “First Meso-American Workshop on Competitiveness”, held in Villa Hermosa, Mexico, and the “IX Meeting of the Meso-American Council on Competitiveness”, which took place in Panama City and provided an opportunity to share the experiences gained with the Competitiveness Support Program (PAC) being conducted by CAF.

Also in 2005, CAF approved a US$ 80 million program for the Republic of Panama to partially finance an infrastructure program that includes substantial investments in road stretches that belong to the integration and development corridors under the Plan. The Corporation participated in several summit meetings of Heads of State and Government of the Tuxla Mechanism for Dialogue and Coordination, which is the forum par excellence to conduct a permanent dialogue at the highest possible level with the purpose of promoting political, economic, financial and trade relations among participating countries, executing regional initiatives, and strengthening cooperation between Mexico and Central America.

## Competitiveness, productivity and international insertion

In its efforts to achieve sustainable development and regional integration, the Corporation actively supports Latin American countries efforts to improve their competitiveness and their insertion in the global economy. CAF’s special programs generate useful knowledge to improve productivity and to design strategies for trade negotiations, providing direct support to a wide variety of specific projects to optimize private and public sector performance in issues related to competitiveness and integration, as well as facilitating access to capital and technology.

These efforts are contributing, through concrete actions, to increase productivity in various economic sectors, to adopt best managerial practices in private enterprises, to develop logistics to reduce barriers to competitiveness, and to disseminate knowledge through events and seminars.

### CAF Competitiveness Program

The third phase of CAF Competitiveness Program (PAC) was initiated in the year 2005, focusing its efforts in the development of clusters and the promotion of entrepreneurial capabilities –two areas in which the Corporation has achieved a significant level of expertise and knowledge. In addition, major contributions were made under PAC to support negotiations of free trade agreements between Andean countries and the United States.

PAC started projects in Colombia to improve the palm oil productive chain; to strengthen the productive and commercial capacity of the cosmetics and cleansing products cluster; and to reinforce

logistics and information systems in the chain of petrochemical products, plastics, rubber, inks and synthetic fibers. In Ecuador, PAC launched projects to increase productivity, innovation and partnership capacity of the clusters of shoe and leather goods in Azuay, automobile bodywork and metal-mechanics in Tungurahua, and wood in Pichincha. In Peru, PAC supported producers and exporters of citric products through a project ensuring their access to North American markets, and initiated activities establish an innovation fund promote and finance business partnership programs.

In the area of promotion of entrepreneurial capabilities, PAC continued its support to the establishment of a Business Incubator in Bolivia and promoted, for the second year row, the Entrepreneurial Ideas Contest. PAC team applied all its experience to the establishment of the System to Support the Creation of Enterprises in Venezuela, which is an initiative that includes universities and academic centers, technological parks and organizations promoting new enterprises. Likewise, PAC is helping Venezuelan enterprises in information technology to access international markets.

**In 2005, CAF focused on developing clusters and building entrepreneurial capacity, thus gaining substantial experience in this area**

In addition, CAF provided support to Andean countries negotiating free trade agreements with the United States by participating in the Negotiations Round Table to Strengthen Commercial Capabilities. During 2005, five rounds were held. Support was provided by conducting studies and projects in public policy (internal agenda, national strategy, public-sector procurements, etc.), promotion of SMEs and productive sectors, and intellectual property. At the same time, CAF played an important role in the dissemination and debate of ideas by organizing four rounds of events that were held in parallel to the negotiations: “Internal Agenda for competitiveness”, organized together with the OAS (Cartagena, 8 Feb. 2005), “Quality, efficiency and logistics for conquering markets” (Lima, 20 Apr. 2005), “Management Tools of partnership projects” (Guayaquil, 7 Jun. 2005), and “Implementation and administration of free trade agreements”, organized jointly with ECLAC (Cartagena, 22 Sep. 2005).

Outside the Andean region, PAC contributed with its expertise to the “First Meso-American Workshop on Competitiveness” (Villahermosa, 16-17 May 2005), the “Ibero-American Seminar on Productivity Development and Business Competitiveness” (Montevideo, 31 May 2005), the “Regional Seminar on Business Competitiveness and MSMEs” (Port of Spain, 17-18 Oct. 2005), and the “Workshop on Clusters of the XI Meeting of the Meso-American Council on Competitiveness” (Panama, 21 Oct. 2005).

### Kemmerer Program: development of financial markets and corporate governance

During the year, the activities conducted by the Kemmerer Program focused on its main strategic goal: improving the quality of security issuers in the region. In pursuing this goal, the definitive version of the *Guidelines for an Andean Code of Corporate Governance* was published in 2005, and the implementation of corporate governance practices in five pilot enterprises in the region was concluded.

With the purpose of promoting the Guidelines, the Program undertook an important plan to participate in multiple events, allowing the introduction of these principles to various actors such as business incubators, entrepreneurs and specialized consultants. In addition, special emphasis was made on the application of the Guidelines in publicly traded and privately held enterprises, banks, and even in small- and medium-sized enterprises. To complement these efforts, the Program published a booklet titled *Corporate Governance: What every entrepreneur must know*, which is available in electronic format in CAF’s website.

Considering the importance of privately held enterprises in the region, important efforts were made in the preparation of a corporate governance manual for this type of enterprises. It will provide, through examples and cases, guidance to consultants and entrepreneurs on the application of best corporate practices. This manual has a complete section on familial management and succession protocols, which serves as a complement to the corporate governance principles.

During the year, the Program team also worked in the planning to implement the second phase of good practices in corporate governance. It will include their application in ten public and private sector enterprises, the design of a software for self-evaluation and the measurement of practices in the five Andean countries.

The Andean Committee of Regulating Authorities of Securities Markets –in which CAF has the status of permanent guest– was created in July through Decision 624 of the Andean Community. This decision is expected to result in more effective actions to promote integration of securities markets in the region.

Finally, as a mechanism to disseminate Kemmerer Program knowledge and experiences, this year was launched the Program's website, available on CAF's Webpage. The site includes various sections such as calendar of events, publications, glossary of terms and links to other institutions of interest, among other things.

### First-Class Ports Program

**By contributing to improve infrastructure management, CAF reduces transportation costs and increases competitiveness of agricultural and industrial products**

The First-Class Ports program is the result of a long lasting collaboration between CAF and the Universidad Politécnica de Valencia (UPV) of Spain. The Program is based on the port management model "*Marca de Garantía*" currently functioning in the Port of Valencia. This model applies the concept that a port is a logistics chain were services are provided by enterprises that represent the links of the chain and quality is limited by the weakest link. Consequently, quality of service in a port depends on relationship management among links of the chain.

At present, this program is being implemented in the five largest Andean ports: Buenaventura and Cartagena in Colombia, El Callao in Peru, Guayaquil in Ecuador and Puerto Cabello in Venezuela, all of which are characterized by the fact that they handle a very high level of general cargo and containers. Together, these five ports mobilize around 3 million TEU, equivalent to more than 65% of the total foreign trade of the countries involved.

The five participating ports have established Quality Councils and their "impulse groups". Membership in each council includes about 25 persons representing the various port communities. In addition, each Council has a technical secretariat that coordinates the group's activities and sets up a database for the port community.

In every port, Quality Councils have internal working groups to re-engineer critical processes. A system with a minimum of three processes is being developed, including vessel operations, flow of import containers, and flow of export containers. In addition, Guayaquil has a working group in charge of banana exports.

CAF and UPV have been working in the development of the institutional framework required for the continued operation of Marca de Garantía. The corresponding legal studies have been concluded, containing concrete recommendations for its organizational structure. The establishment of an entity managing the quality of port operations depends only on the approvals of CAF and of the Marca de Garantía Foundation in Valencia, Spain.

Even though the benefits resulting from the adoption of Marca de Garantía for Port Services will materialize in the upcoming months, it is already possible to observe substantial improvements in the ports' performance which are the result of a better organization of ports' authorities and the process analysis associated with this program.

### Research Program in Development Topics

The main objective of this program is to establish a relation with the academy in the region, financing research projects on development-related topics. Thus, support is provided to Latin American researchers, while CAF benefits from the implementation of the activities foreseen in its development agenda. The Program's initial calls for papers during its first four stages received an annual average of 70 proposals from 14 countries. Based on these works, the Program launched the Report on Economics and Development, a yearly publication dealing with issues of relevance for the regional public policy agenda in a systematic and comprehensive manner. In 2005, the fourth stage of this program was concluded.

This year's call for papers resulted in the selection of seven research proposals carried out by the authors in their own research centers. The proposals focus on issues related to productive transformation, such as productivity, regulations, diversification strategies, and cluster development, among others. The findings of these studies have been shared with policymakers in the region through round tables and international seminars, contributing to the decision-making processes, while promoting dialogues between academic and public sector institutions. In addition, the Program team published two new issues of the biannual journal "*Perspectivas*" containing these studies. The topic of fifth call for papers for 2006 is "Challenges to social inclusion".

## CAF's social agenda: towards an inclusive and equitable human development

The spread of global poverty is increasingly leading to non-harmonious coexistence among the inhabitants of the planet. At the same time, millions of people have no access to basic infrastructure services. They are totally excluded from the new available technologies in the middle of an era of knowledge and information. They work in jobs –if they happen to be employed– that hardly allow them to support themselves. They are almost totally uninvolved in their communities. Latin America is not excluded from this reality, because the levels of macroeconomic stability, financial growth and commercial openness achieved over the last 20 years have not led to any significant improvement in the people's living conditions. Indeed, Latin America continues to be the region with the greatest degree of inequality worldwide, and while the fall in poverty this past year is praiseworthy, this scourge continues to affects 213 million Latin Americans, almost 90 million of whom live in extreme poverty conditions and survive on less than one dollar a day.

CAF, in alliance with a host of other institutions, in 2005 expanded the activities it has been undertaking in the past to enhance the living conditions of thousands of people. The experience has been a highly enriching one, and the projects and programs approved in the social sectors during the year stand out for being oriented towards social equality, for being innovative and scalable, for encompassing a territorial vision and for producing a highly favorable impact on the population beneficiary of the programs. In addition, the institution continued its highly recognized activities in the area of cultural, social and community development, increased its contribution to employment generating sectors, such as SMEs and micro-enterprises and continued its efforts toward encouraging proper governance through the development of leaders with civic and democratic values and of solid institutions that will guarantee responsible participation by all social players.

### Social Investment in member countries

In 2005, CAF increased its efforts to support social investment in its member countries, approving the amount of US$ 288 million. These efforts were focused

**Through social investments, CAF contributes to improving basic services, infrastructure, productive capacity and living standards of the poorest communities in the region**

on technical and financial assistance to four sectors: drinking water and sanitation, rural development, education and health. It should be noted that CAF's social portfolio accounts for 36 percent of its overall portfolio and totals US$ 2,550 million.

This year was also marked by the development of outstanding innovative forms of financing. In Colombia, for example, the Drinking Water and Sanitation Program of the Department of Cesar amounting US$ 42,5 million from CAF, is intended to promote a more efficient and equitable use of royalties obtained from the coal sector. The loan, guaranteed with future royalties, will improve sector management and build aqueducts and sewer systems in several municipalities. In Ecuador, the PRAISE Program aims to safeguard the resources earmarked for the social sector by directing its objectives in coordination with the different actors. CAF is developing an innovative model for structuring the operation and its financing, involving the use of present and future revenues from coal royalties to open up fiscal space.

*Drinking Water and Sanitation*. Since its beginnings, CAF has accumulated a vast experience in financing infrastructure to increase drinking water and sewage services coverage. Currently, however, the sector has acquired a new dimension and a new social perspective. Consequently, efforts are now underway to develop programs and projects with a high human, social and environmental impact and geared towards innovation, inclusion and sustainability. Emphasis has been placed on providing access to services for the most vulnerable sectors of society, on enhancing the quality and efficiency of such services by improving the performance of operators, and on ensuring sustainable investment.

CAF approved US$ 104,5 million for operations with high level of complexity and technical challenge in 2005. The design and structuring of the operations have resulted in innovative solutions and have proved to be a learning process for the Corporation and the expansion of possible operations to the country.

The support project for expanding the coverage and development of the drinking water and sanitation systems in the Metropolitan District of Quito is a clear example of this effort. This project, which is being undertaken with a US$ 25 million contribution from CAF, benefits 700,000 people and represents an innovative working scheme because it involves funding an initiative carried out by the public enterprise, EMAAP-Q, with the sovereign support of the nation.

*Rural Development*. This year also witnessed the continuation of the Sustainable Rural Development Project for the Semi-arid areas of Lara and Falcon States in Venezuela (Prosalafa II). The project was co-financed with the International Fund for Agricultural Development (IFAD), with whom CAF has a cooperation agreement for over 23 years. This multidimensional operation contributes to improving the quality of life of small producers communities by promoting beneficiaries empowerment and the sustainability of the advancements in their social organization, productivity, income increase, management of natural resources and technology transfer.

Likewise, within the framework of the ties of cooperation between the IFAD and the CAF, the Corporation continued its support to 17 projects –some under execution, others fulfilling contract-related requirements, and rest are subscribing their contracts– at a total cost of US$ 257 millions. These programs have been effective in helping rural farmers, breeders and fishermen to be better organized, to enhance their capabilities to manage their own resources, to boost their productive capacity and to improve their quality of life.

*Education*. In 2005, CAF earmarked resources for programs and projects designed to boost the quality of –and investment in– education as a powerful tool in fighting poverty, in building more participatory societies and in promoting equitable and inclusive development in an environment of democratic governance. In this respect, a total of US$ 15 million was approved for upgrading technical and technological education in Colombia, while in Venezuela an amount of US$ 20 million from the 2003-2004 Multisectoral Public Investment Project was reassigned to improve the physical conditions of 250 schools located in depressed socioeconomic areas. In addition, studies are underway to determine the feasibility of supporting a policy of universal pre-school education in Venezuela. To this end, technical cooperation resources have been approved to support the Ministry of Education and Sports to identify the most appropriate strategies consistent with the commitments of the United Nations' Millennium Goals.

Meanwhile, in 2005 CAF published the second edition of the "Andean Agenda for Education" to promote the debate and reflection on educational issues in different areas. It also witnessed the beginning of the series entitled *Working Documents on Social-Educational Development* and the signing of cooperation agreements with the UNESCO and the Organization of Ibero-American States (OEI), as one way of contributing to greater awareness and understanding of the intricacies of the educational systems of CAF shareholder countries.

Meeting of the Bi-national Spain-Ecuador Debt Swap Committee (8 March 2005), with CAF at the helm of its Technical Secretariat.

It should be noted that in 2005, CAF received two recognitions for its technical and administrative efficiency. The Cooperation was selected to oversee and administer the Mercosur Educational Fund (FEM), which is the first resource-providing fund of this important regional integration process. The Corporation was also chosen as responsible for coordinating, managing and administrating the Debt-for-Social Investment Swap Program –particularly education– between the Kingdom of Spain and the Republic of Ecuador.

### CAF manages fund for debt conversion into social investments

In March 2005, the governments of Ecuador and Spain signed the Program for Debt Conversion into Public Investments that established a US$ 50 million Fund, whose administration and management have been entrusted to CAF. This binational agreement is an innovative instrument that the Kingdom of Spain is promoting to invest in Latin America and support regional development. The purpose of the Fund is to channel resources –which otherwise would have serviced foreign debt– to co-finance projects improving living standards of vulnerable communities.

The selection of CAF to manage the Fund for Debt Conversion was based on the Corporation's vast experience in supporting sustainable development in Ecuador, which ensures efficient and effective performance in facing this new challenge. CAF's responsibility is to provide technical assistance to the Binational Committee –the highest authority of the bilateral agreement– for the evaluation, selection, administration, execution and monitoring of hydroelectric projects under the Clean Development Mechanism (CDM), and education projects.

Both governments agreed to swiftly select the projects and programs to be financed with the Fund as to achieve the greatest impact, to reach the beneficiaries directly and improve the standards of living of the people reached.

It is worth noting that, at its first regular meeting, the Binational Committee approved four of the ten education projects under study adding US$ 1.8 million, equivalent to 9.3% of the resources earmarked for this sector.

*Health*. During 2005, CAF defined strategic guidelines to support programs and projects in the health sector. In line with the UN's Millennium Goals, these guidelines prioritize the channeling of investments to reduce mother and infant mortality rates, and infancy protection and care. A total of US$ 24.7 million in funding was approved, jointly with the IDB, for Colombia's Expanded Immunization Program to ensure appropriate levels of immunization among children 5 years of age or less. Additionally, Venezuela received non-reimbursable technical cooperation to conduct studies on healthy housing in areas affected by hyperendemic diseases, such as leprosy, in the states of Apure, Cojedes and Portuguesa.

## Cultural and Community Development Program

In 2005, CAF continued the allocation of resources to the Andean countries to build and strengthen skills and capabilities in communities with scant resources. Special emphasis was placed on the building of alliances with strategic partners to ensure the sustainability of the projects and improve and expand the overall performance of CAF. Reference should be made to the agreements forged with the Spanish

Agency for International Cooperation, Repsol and the Codespa Foundation of Spain, and with Italy's international cooperation bodies. Nationally, the active participation of the public sector, particularly at the local and regional level, have been a crucial factor worth duplicating. The private sector, including banks, businesses as well as CAF, has also participated actively, as it strives to fulfill its corporate and social responsibility.

The initiatives being promoted encourage development and training in the areas of choral-symphonic music, sports, cultural heritage and local cooperation, with an ultimate goal of building community models for organization and for social and productive self-management. In all these areas, the basic strategy is multidimensional. It is aimed at strengthening and uniting the fabric of society –particularly in the most vulnerable sectors (children, youths and women) of the poorest population groups (peasants and indigenous populations). Consequently, it must be implemented in conjunction with socially reliable players, partners and operators who are capable of boosting the impact –and contributing to the sustainability– of these initiatives. They are channeled through a cultural, productive, social or any other kind of medium that facilitates the development of a process to obtain better citizens and the promotion of an effective exercise of social, political and economic rights.

Gala concert in Caracas, Venezuela, marking the CAF's 35th Anniversary. More than 800 artists were on stage, including members of the Latin American Youth Symphony Orchestra, the Andean Youth Choir and the National Symphony Choir of Movimiento Coral Cantemos, for the delight of a large audience that applauded them for several minutes.

With respect to *music education*, the Itinerant Andean Conservatory (CAI) and the workshops of the Andean Choir Voices (VAC), were strengthened not only through the educational process for local students and teachers in the Andean countries but also with the its expansion and inclusion of member countries in the Corporation's *C Series*. Likewise, the concert held to celebrate the Corporation's 35th year also marked the launching of CAF's Latin America Symphony Orchestra, directed by Master Claudio Abbado. Furthermore, choral-symphonic concerts were held in Ecuador, Colombia and Bolivia, thus highlighting the success of the Social Action Program for Music in these countries.

With regard to *Heritage*, a regional alliance was forged with the Spanish Agency for International Cooperation (AECI) for the joint implementation of cultural heritage projects in the Andean countries, particularly the development of hands-on schools to train youth people in technical and art restoration skills, helping them accessing the labor market and generate income.

In the area of *Sports*, projects were continued in Peru, Colombia, Bolivia and Ecuador, with football serving as a prevention and education tool and as an instrument to promote social organization and community development.

As for *Local Cooperation*, several of the community projects undertaken in conjunction with

**CAF promotes a broad-reaching agenda for human development to invest in community organization and capacity building, to support sectors facing limited access to financial resources**

organized communities, local and regional governments, other public and private agents and bilateral and multilateral cooperation institutions, entered their second stage and were continued to develop a model of self-management and institutionalization. Almost all of these projects were marked by increased participation in the development of joint agendas and project portfolios at the municipal level, improving the culture of production building new capacities in areas such as health, education and community saving, contributing to build and strengthen the fabric of society and fighting against inappropriate living conditions of the population.

### SMEs and Microfinance

Micro, small and medium-size enterprises (SMEs and Microfinance) represent a highly significant segment of the business sector in Latin America. The largest amount and the major segment of private business initiative in the region belongs to this sector. It makes a highly significant contribution to ensuring equitable economic growth, thanks to its large capacity to create new jobs. SMEs and Microfinance, however, have limitations to access to financing, to markets, and to strong managerial services, preventing them from fully developing their ability to create jobs and to foster economic well-being.

CAF believes that economic development must essentially be matched by a more equitable distribution of benefits. It supports initiatives contributing to remove some of the obstacles facing these enterprises on the basis of three strategies: facilitating the access to capital of sectors with limitations, supporting the internationalization of SMEs and promoting the insertion of SMEs and Microfinance in CAF-sponsored projects.

*Access to capital*. To facilitate the access of micro-enterprises to resources, CAF supports microfinancial institutions providing these enterprises with saving and loans services. This support is provided through alternative financing facilities, such as stock participation and subordinate loans to help them strengthen their equity base, loans and credit lines to expand their operations, and partial guarantees to support bond issues allowing them to access capital markets. In addition, technical assistance programs have been implemented to help them strengthen their institutional base, and consulting services are provided to assist in the development of adequate regulatory frameworks and support the sustainable growth of microfinance.

In 2005, CAF incorporated several new clients, and currently supports thirty five microfinance institutions in eleven Latin American countries. In total, these institutions serve around two million micro-enterprises. On the International Microcredit Year, CAF promoted forums and workshops to encourage the debate on topics such as the creation and innovation of new products and services, the promotion of greater disclosure to improve their competitiveness, means to achieve a sustained reduction in costs for micro-entrepreneurs, better regulation and greater support for the rural sector, among others.

To promote the strengthening of the equity base of SMEs, CAF administers the Business Investment and Development Fund for Small- and Medium-Size Enterprises (FIDE). In alliance with local, public and private institutions, FIDE has invested in new and different initiatives, such as technologies, clean generation of energy, agriculture and software export. To facilitate the access to credit of small- and medium-size entrepreneurs, and other sectors such as the rural and educational sectors, CAF is currently developing innovative financing mechanisms and strategies to grant credits to small- and micro-farmers within their own areas, such as the reinforcement of credit guarantees issued by national guarantee systems or the structuring of trust funds in association with companies in the agriculture industry.

*Internationalization*. One of the main constraints facing small and medium-size enterprises in the region is their difficulty to gain access to international markets, explaining their low participation in the countries' exports. CAF has developed joint programs with academic institutions and professional business associations to identify markets and to strengthen marketing and export capabilities. Agreements have been made with academic or business institutions, such as the Wharton School of Business at the Pennsylvania University (USA), the Universidad de los Andes (Colombia), the Universidad del Pacífico (Peru) and the Venezuelan Confederation of Industrialists.

*Insertion*. With regard to this third line of action, CAF has successfully included a component linked to the development of SMEs and Microfinance directly or indirectly associated with projects to be financed. The most successful operations undertaken in the area of insertion have been in road construction and irrigation projects.

Enrique García, Executive President of CAF, and Juan Carlos Durán, President of Colombia's National Guarantee Fund (FNG), sign an innovative risk participation agreement.

### Financial Innovation to support SMEs

In 2005, CAF signed a risk sharing contract for US$10 million with Colombia's National Guarantees Fund (FNG) where the Corporation will partially cover guarantees issued by the FNG to Colombian banks. The objective is to promote credit issuing for working capital to Colombian SMEs. Through this operation, the banks will cover certain risks and could grant US$80 million in new loans that will benefit approximately 5,600 small- and medium-size enterprises. This reinforcement operation –the first of its kind to be undertaken by CAF– is intended to promote the strengthening of the private sector, competitiveness and productivity in Colombia and contributes to equitable economic development. This innovative and sustainable operation, whose effects are highly visible, will facilitate access to credit for a large number of companies that, without the guarantees of the FNG, would otherwise not be able to obtain credit from the financial system because they do not have adequate guarantees.

## Governance Program

During the last decade, a change in focus has taken place in Latin America regarding the need to have strong, competent public institutions providing citizens with the public assets and commendable services they are demanding. In 2005, CAF consolidated its effort in the area of democratic governance on the basis of four lines of action: the recovery of public ethics, politics, institutions, and the value of citizenship within the specific context of the State. This framework encompasses the execution and consolidation of CAF´s four regional programs with national coverage through strategic associations with important institutions. In addition, a fifth program, which is geared toward public institutions and their functions within the framework of democratic governance, was launched in Bolivia.

*Program of Governance and Political Management*. The objective of this program is improve management of a contemporary State and to improve the quality of public administration by means of developing a critical number of leaders and their support teams at the institutional level, in public administration and policy dynamics in the Andean countries. To day, five groups have graduated in Bolivia, three in Colombia, four in Ecuador, three in Peru and three in Venezuela, bringing the number of graduates to 2,744. This program is being conducted in association with the George Washington University and with prestigious educational local institutions. In Bolivia, the partnership is with the Universidad Privada del Valle, in Colombia with the Rosario and Francisco de Paula Universities and the Universidad Autónoma de Bucaramanga, in Ecuador with the Universidad Católica del Ecuador and the Universidad de Guayaquil, in Peru with the Pontificia Universidad Católica del Perú, and in Venezuela with the Universidad Católica Andrés Bello.

*Program of Leadership for Transformation*. This program identifies and develops natural leaders to exercise their citizenship and perform their community duty with responsibility, knowledge and aware-

Within the context of the Leadership for Transformation Program to increase social participation and inclusion, CAF is promoting training courses for new natural leaders to provide them with a comprehensive vision of their country's reality and civic-democratic values.

ness of the reality of their countries with a national vision and civil and democratic values. In 2005, a second version of the program, which was implemented in Bolivia, Colombia and Peru, produced a total of 3,926 leaders who were fully trained or are being trained. The program lasts six months and is conducted with educational institutions, such as the IDEA Foundation in Bolivia, the Advanced Institute of Public Administration in Colombia and the Government Institute of the San Martín de Porres University in Peru.

*Efficient Municipalities Program–MuNet*. This program involves the transfer of best practices to municipalities in the areas of land titles registration and electronic government by sharing knowledge and successful experiences obtained in similar sociopolitical contexts. This program is conducted in collaboration with the OAS and the Canadian International Development Agency (CIDA). At the beginning of the year, the first workshop on electronic government was held at the headquarters of CAF. The workshop was attended by over 100 international guests belonging to the municipalities participating in the program. The electronic government program currently includes 21 municipalities throughout the region and is geared toward the implementation of a portal known as Municompras, while the land title registration program covers five municipalities, which are currently preparing the final projects before signing agreements with the mayors of those municipalities.

*Program on Tools for Governance and Consensus Building*. This program was initiated in Bolivia and Peru in 2004, providing strategic players of the public sector and of civil society traditionally in confrontation, with advanced techniques in conflict resolution and with modern tools of negotiation, strategic communication, leadership and persuasion. The second stage of this program is slated to end in 2006.

*Institutional Building Program.* The program is intended to encourage direct citizen involvement in public institutions in areas such as sectoral reform, fiscal decentralization, standardization of the municipal land title registration in and civic education. In 2005 it was initiated in eight institutions in Bolivia.

## Sustainable environmental agenda

During 2005, CAF continued with activities oriented to ensuring the best possible use of the region's natural resources, its value and preservation while tapping this resources to derived benefits which can be distributed in an efficient and sustainable manner.

The process of reviewing CAF's environmental strategy was further advanced –in line with the increase in the number of shareholder countries and with the expansion of its operational base– and CAF's System of Environmental and Social Evaluation and Follow-up of Operations was renewed. The purpose of the System is to guarantee the inclusion of environmental and social principles in the various phases of the credit cycle, in order to ensure that the operations undertaken are environmentally sustainable and socially responsible. In addition, the development of support tools, such as the "Manual of environmental and social management for operations in infrastructure, industry and institutional services" were initiated, and the development of the SIGAS (Information System for Environmental and Social Management), a computerized tool designed to speed up the handling of documentation generated during the evaluation process, and of the EGALS (Evaluation of Environmental, Labor and Social Management), which is designed to facilitate the evaluation of the CAF's corporate clientele, was consolidated. Likewise, the publication module for projects dealing with the Condor Geographical Information System was completed.

With its credit approvals, CAF promotes the preservation of habitats and ecosystems through appropriate management plans.

The holding of the Fifteenth Meeting of the Forum of Environment Ministers of Latin America and the Caribbean (Caracas, Nov. 2004) is also noteworthy. At this event, CAF called for collective responsibility with regard to the topic of the environment and stressed the importance of biodiversity, the urgent need for change in consumption patterns and in the management of natural disasters, among others. It also insisted on the need for countries to increase investment in the environment and to change environmental paradigms in those which, in the words of Alfredo Sfeir Younis, need not only to combat contamination but also to create awareness in the contaminator to serve as an instrument for change.

## Latin American Carbon Program (PLAC)

The main purpose of PLAC is to contribute to the development of the carbon market, to create new financial instruments and mechanisms and to promote the participation of business and productive sectors in this market. Its major achievement in 2005 is the development of the Ibero-American Carbon Initiative with the Kingdom of Spain. This initiative consists of a fund designed to develop and implement projects of the Clean Development Mechanism (MDL) set out in the Kyoto Protocol. CAF has pledged to secure the reduction of nine million tons of carbon emissions for Spain. Both the buying and selling member country will benefit from this effort.

In 2005, PLAC evaluated over 100 potential MDL projects in different productive sectors, such as hydroelectric, biogas and wind energy sectors. CAF also made significant contributions to the development of the carbon market with the creation of two new methodologies, one which has been approved and the other which is in the process of approval. It should be noted that the first credit contracts for the purchasing and sale of carbon have already been signed.

PLAC continued its support to climatic change offices of member countries through different regional events in institutional strengthening and global positioning. In conjunction with the Ministry of Housing, Territorial Organization and Environment of Uruguay, PLAC held the third annual event on climatic change in Latin America and the Caribbean in Punta del Este in Mar. 2005. The event was attended by representatives of national agencies responsible for climatic change in 15 countries of the region and by international representatives of the public and private sectors of Holland and Canada, of the International Emissions Trading Association (IETA), of consulting firms and of various other institutions. This event is considered the main event in the region to update participants and to document the lessons learned by Latin American actors. Also, a workshop to Latin American climate change to support negotiators (Caracas, Nov. 2005) resulted in a concrete agreement. The countries then unanimously presented it to the methodology panel of the Climate Change Secretariat at the eleventh conference of the parties and at the first meeting of the parties (CoP 11 / MoP 1), which was held in Montreal at the end of 2005. Specialized technical workshops were held, and direct support continued to be provided to CAF´s member countries´ climate change offices through bilateral technical cooperation programs.

In 2005, PLAC also identified and developed over 15 projects to fulfill and complete commitments set in the CAF-Netherlands CDM Facility fund, created in 2002. The projects would supply 16 million tons of carbon emission reductions.

Finally, as part of its commitment to sustainable development, CAF is prepared to finance renewable energy and energy efficient projects with or without a carbon component. At present, different modalities of financial support to qualifying projects are being assessed, as a complement to CDM.

## Biodiversity Program – BioCAF

The general purpose of this program is to promote the use of biodiversity and genetic resources through sustainable environmental practices and consists of several subprograms, whose activities are described below.

*Biocommerce*. The regional project entitled “Biodiversity-based Business in the Andean Region” is being fully developed with resources provided by CAF, the Global Environmental Facility and countries’ counterpart funds. Participating in the project are the Ministry of Sustainable Development of Bolivia, the Ministry of Environment, Housing and Territorial Development (MAVDT) and the

**Latin America has made substantial progress in wild fauna protection, although it is necessary to foster exchange of knowledge in this area for greater sustainability**

Alexander von Humbolt Institute of Colombia, the Ministry of the Environment and the CORPEI of Ecuador, the CONAM and the PROMPEX of Peru and the Ministry of Science and Technology and Ministry of the Environment and Natural Resources of Venezuela. The results of the consultations are beginning to show specific trends in the needs of region: sectors and markets development, legal framework reform and policy prioritization, among others.

During the year, CAF promoted the strengthening of biocommerce. In Venezuela, it supported the "First Meeting for Exchange, Information and Experience on Biocommerce between Colombia, Ecuador, Peru and Venezuela" that was held in Caracas in February 2005. The meeting shared experiences and contribute methodological and conceptual ideas for the development of Venezuela's own national biocommerce program. In Colombia, CAF supported the implementation of the Strategic National Plan for Green Markets, under the MAVDT, through the organization of the Bioexpo Colombia 2005 event in Medellín. Groups of producers and groups developing green market initiatives in the Amazon, Pacific, the Atlantic Coast and the Coffee Axis regions attended the event. Thus, an important contribution was made to the promotion and dissemination of ecological and environment-friendly products nationwide, while other businesses were promoted at both the commercial and financial levels. CAF signed an agreement with Costa Rica's National Institute of Biodiversity to assist the development of the initial phase of the creation of Costa Rica's National Biocommerce Program. Finally, the book "Bio-commerce in the Andean Subregion. Development Opportunities" was published, giving an overview of the promotion initiatives and the most relevant experiences gathered in each country.

*Biotechnology*. This year CAF, the Iberoamerican Consortium for Education in Science and Technology and the Inova Center of Brazil's Universidad de Campinas, organized the First Encounter on Undertakings in Science and Technology for the Socioeconomic Development of the Region. The event provided the opportunity to present business plans of Andean and Brazilian entrepreneurs in biotechnology to international investors. CAF co-edited with ECLAC the book "Biotechnology for the sustainable use of biodiversity: local capacities and potential markets". It is the result of a research that highlights the great potential of the Andean countries in the global markets. It suggests the development of technological and institutional capabilities in the Andean region and strategic guidelines for national and multilateral policies.

*Negotiators*. This subprogram involves the support granted to international negotiators participating in regional or international forums where debates are held on commercial and environmental issues. One of the topics discussed during the year concerns the protection that should be granted to the traditional knowledge of indigenous groups with respect to biodiversity and cultural matters. With the collaboration of the Secretary General of the Andean Community, a team of indigenous experts was contacted and their first paper, "Elements for the specific protection of collective and integral traditional knowledge from an indigenous perspective", was published. The paper includes the adoption of positions by organizations representing the natives and provides an overview for designing an Andean system for the protection of the knowledge of these indigenous groups.

*Conservation*. One of the purposes of BioCAF is to promote ecosystem conservation initiatives through operations undertaken by CAF. Hence, within the framework of a joint operation with the Venezuelan company "CVG Electrificacion del Caroní", technical cooperation was provided to the Indigenous Federation of Bolivar State for the conservation of the Parque Canaima. Its purpose is to develop a strategy for holding consultations with indigenous communities and to consolidate the "Life Plan of the Pemon", the indigenous people living in the area.

Also, an electric transmission line financed by CAF and to be built by Interconexión Eléctrica S.A. of Colombia (ISA) in Bolivia led to the identification of yet another opportunity. It requires the preparation of a proposal for the conservation of bofedales (saturated pasture land) and the support to the local indigenous community living in the area affected by the project.

A further activity carried out within the framework of the Program was the signing of a technical cooperation agreement with the National Institute of Natural Resources of Peru for the development of pre-investment studies, which will be used to back up the implementation of the country's National Reforestation Plan. Likewise, an agreement was signed between CAF and the governments of Colombia and Peru to assist with an initiative for the integral and sustainable management of forests found on the border between Carapace and Rio Lagoon. This initiative is to be developed with the participation of local communities.

## Sustainable Development Program for Financial Institutions

This program was created by CAF to promote sustainable development in the financial sector by identifying the risks associated with the lack of information and the opportunities inherent in the emerging environmental service sector. The scoping paper "Document for the Latin-American Work Group for the Financial Initiatives Program" being developed within the framework of the United Nations Environmental Program (UNEP IF) was published in February by CAF with the title "Sustainable Financing in Latin America". It identifies specific environmental and social research opportunities in Latin American financial institutions. Moreover, with the purpose of internalizing these principles in the industrial and financial sectors in the region, CAF began planning various activities, which include the training of clients and partners of the Corporation through workshops, publications, local and international events relating to the financial sector and sustainable development.

## Prevention and reduction of natural disaster risks

The Andean Program for Disaster Risk Prevention and Mitigation (PREANDINO) ended its first stage and an institutional report was prepared on the achievements of the program. In 2005, the organizational study of the International Center for Research on the El Niño Phenomenon (CIIFEN) was completed, the regional platform was established and the necessary sectoral products and requirements that could be attended to by this center and by the institutions belonging to the network responsible for such purposes were specified. In addition, support was provided for the new direction of the program with the development of an initial survey on the investment requirements for the prevention and reduction of natural disaster risks with the participation of the national and sectoral institutions of the different countries. An institutional document resuming the activities of the program was also published.

The program in 2005 also assisted in the development and consolidation of institutional, legal and planning capabilities to enable the countries of the region, with the support of their national planning agencies, to fully assume the implementation of the program in 2006 where need for investment to reduce risk will be identified.

In 2006, priority will be given to reinforce countries` natural disaster risk management in their planning processes, to enable them to identify and to incorporate risk prevention projects and financing requirements in their respective public investment systems. CAF will continue designing financial products and services increasingly tuned to risk management requirements, consistent with countries priorities.


*Above:*
Participants at the Seminar *Business in Latin America* that is held every year to contribute to strengthen the region's position in foreign markets.

*Below:*
CAF's Executive President delivers a speech at one of the workshops held in several countries in 2005, on how to reactivate economic growth in Latin America.

## Seminars and events

During 2005, CAF participated, organized and/or sponsored various integration-related seminars and events to strengthen its own position and of its member countries in different sectors. The most important were the following:

• *Business in Latin America* (FEB/05). This seminar, organized jointly with the magazine Foreign Policy, included the publication of a supplement on the Andean countries, which was distributed at the World Economic Forum in Davos, as well as a publication containing writings and articles on the political, social, economic and financial issues discussed during the meeting.

• *Workshops on Reflections to Resume Growth* (FEB-MAR-JUN-JUL/05). CAF presented the results of the first edition of its Economic and Development Report (RED 2004) entitled "Reflections to Resume Growth: International Insertion, Productive Transformation and Social Inclusion" at forums held in Lima, New York, Bogotá, Caracas, La Paz and Quito. These forums were attended by prominent academicians and representatives of the public and private sectors.

• *Innovations in Microfinance: Scope and Challenges* (MAR/05). Held within the framework of the International Year of the Microcredit, this seminar-workshop brought together in Caracas, Venezuela, the highest authorities of microfinance institutions, clients of CAF, and a group of prominent experts in the area of microcredit, to develop a shared vision of the future of the industry, with the purpose of seeking opportunities for the sectors with limited access to capital.

• *Reflection Workshops on Development Policies* (APR-JUN-SEP-NOV/05). As in previous years, CAF organized a series of reflection workshops on relevant issues relating to the region's public policies. The forums held included "Commercial Liberalization, Macro-economic Fluctuation and Contingent Protection in Latin America", "Impact of the Different Routes of International Insertion for Latin America", "Commercial Policy and Foreign Direct Investment: Implications for Latin America", "Workshop on Public Policies" and "Seminar on International Insertion". These events were attended by experts from the academy, policy-makers and representatives of the private sector.

• *V Encounter of Former Latin American Presidents* (MAY/05). Held in Cartagena Colombia, this summit developed a global agenda for the region and featured the main issues addressed at earlier summits, particularly those relating to competitiveness, culture, the social agenda and governance. The former Latin American presidents attending the meeting were presented with the book "Cultural Public Policies" corresponding to the IV Encounter.

• *I Meso-American Workshop on Competitiveness* (JUN/05). The purpose of this meeting was the development of a common vision of the eight countries of the Meso-American region allowing them to take advantages of –and to build on– their potential to boost their competitiveness and to work jointly to increase trade and investment among themselves. The event was attended by representatives of the public and private sectors.

• *Strategies to Finance Higher Education in Latin America* (AUG/05). Organized jointly by the Institute for Higher Education in Latin America and the Caribbean, the UNESCO and CAF, this seminar brought together experts and chancellors of the leading universities and higher education centers of Latin America. The aim of the meeting was to analyze, and to hold debates on the present and future of financial sources to higher education.

• *IX Annual Conference of the Andean Development Corporation on Trade and Development in the Americas* (SEP/05). As an important platform for debate and analysis with political players of the USA and the Andean countries, CAF, in conjunction with the Inter-American Dialogue and the Organization of American States (OAS), organized this event in Washington, D.C. The event brought

**With participation of all sectors, the events and seminars organized and sponsored by CAF facilitate negotiations, consensuses and decision-making processes, while strengthening Latin America's position on the international scene**

together political and economic leaders and members of the academic community and of the media who discussed the importance of economic, political and financial ties of bilateral and multilateral nature.

• *Implementation and Administration of Free Trade Treaties: Challenges to Governments and Business Groups* (SEP/05). With the purpose of assisting governments, CAF held this meeting in Cartagena, Colombia, jointly with the Economic Commission for Latin America and the Caribbean (ECLAC). The meeting was directed at business leaders and congress members of Colombia, Ecuador and Peru and was aimed at generating debate on ways to foster consensus building on public policies and on the development of tools allowing countries to take full advantage of the benefits offered by FTAs. This event was carried out within the framework of the XII round of FTA negotiations.

• *X Annual Encounter of the Latin America and Caribbean Economic Association*, (LACEA) (OCT/05). This meeting, co-sponsored by the CAF, was held in Paris and served as the setting for the exchange of ideas and proposals on public policy in different areas of global interest. The meeting also addressed a series of social and economic issues relating Latin America of interest to European academicians and officials and to thinkers and intellectuals from around the world.

• *International Dialogue on the Commercial Strategies of Latin America, Regional and Multilateral Initiatives* (OCT/05). Organized jointly by The International Centre for Trade and Sustainable Development and CAF, this event held in Geneva analyzed commercial negotiation strategies of Latin American countries and, in particular, to harmonize regional and multilateral initiatives were countries of the region participate.

• *VIII Microenterprise Forum* (OCT/05). This meeting was organized in Santa Cruz, Bolivia, by the Inter-American Development Bank, the Secretariat of the International Year of Microcredit as part of the United Nations Capital Development Fund (UNCDF) and CAF. The purpose of the event was to highlight the prospects of Latin America and review the results achieved during the International Year of Microcredit. The meeting was attended by the national microcredit committees, by finance ministers, Central Bank presidents, experts in legal and regulatory policy and the private sector.

• *Andean Evening* (NOV/05). Within the context of the Seventh Latibex Forum, which was held in Spain, CAF organized this meeting with Latin American companies and important figures of the international financial community. The purpose of the event was to publicize and promote business opportunities in the countries and companies of the region. The panelists, who came from the public and private sectors, spoke at length of the investment opportunities available and of the most rapidly developing economic sectors.

• *Latin America in Global Trade* (DEC/05). This workshop presented the results of the second edition of the Economic and Development Report (RED 2005), entitled "Latin America in Global Trade: Winning Markets" to the members of CAF's Board of Directors and representatives of the economic and academic fields. During the event, the existence of barriers limiting free trade in goods and services among the countries were highlighted, and critical aspects of trade negotiations were analyzed.

• *Seminars for Reporters, Editors and Owners of Social Communications Media*. To strengthen governance, in 2005 CAF continued training journalists and managers of the mass media in topics of interest to the region. In thirteen events, 401 journalists, editors, columnists, media

Part of the group of the 74 directors, editors, TV anchormen and journalists from Latin America, the United States and Spain who gathered in Mexico to debate on news quality in mass media and the new social demands in Latin America.

directors and academics specializing in communication attended. The Training Program represented seven events, while the Reflection Program represented six activities, including the "Round Table on Governance in the Andean Countries" and the "XI Euro Latin-American Communication Forum, the EU and Latin America, between Spain and Portugal". All these activities were carried out jointly with the New Ibero-American Journalism Foundation and were complemented by events staged by other allies, such as the Grupo de Diarios de America, the International University of Florida and the Venezuelan Chapter of the Institute of Press and Society.

## Institutional Publications

In 2005, CAF, through it various publications, continued to support the implementation of a renewed regional development agenda by internally and externally disseminating knowledge and information on topics to help strengthening a Latin American integration process and providing a framework for sustained development in its member countries. The book *Latin America in Global Trade. Winning Markets* is the second part of the series, Economic and Development Report (RED2005), was published. Given the impact of the earlier edition of RED2004, *Reflections to Resume Growth,* an English version was distributed to expand the key audiences interested in gaining access to proposals relating to the problems affecting the region. The year 2005 also saw the publication of two books, *Perspectives: Analysis of Critical Themes for Sustainable Development* (a six-monthly publication of CAF) and *Sectoral Policies in the Andean Region. Lessons and Proposals*, both of which have placed the Corporation within the framework of the international debate on public policy.

As a strategic contribution to regional integration, the book "*The Commitment of CAF to South American Integration*" was published. The book highlight the impact of the activities of the Corporation in the area of physical infrastructure, particularly in the fields of road construction and energy, as well as the scope of the projects developed within the framework of the IIRSA Initiative. In addition, as regards infrastructure, the Sectoral Reports continued to be published, and 2005 saw the appearance of the following *Ecuador: Analysis of the Telecommunications Sector and Colombia: Analysis of the Transportation Sector*.

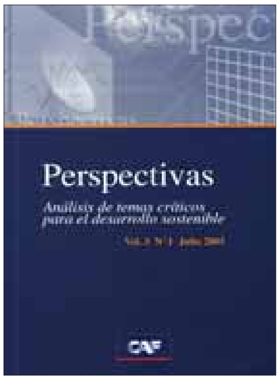
To expand the dissemination of information on the work that the Corporation has been conducting over the past five years in the areas of productivity and quality, the Corporation also published reports on the *CAF Encounter for Competitiveness*. This event was held with the purpose of presenting the lessons learned from the projects relating to the Competitiveness Support Program. In addition, with the intention of disseminating information on the achievements made and on projects that have been successful, CAF also published the book *Technical Cooperation: Impulse for Development*, which highlights the impact of the work being done by the Corporation in different areas of action with the use of its technical cooperation resources. Likewise, within the framework of the International Year of Microcredit, the Corporation held a meeting with clients to conduct in-dept study on topics of interest and to develop a shared vision of the future. This meeting led to the publication of *CAF and Microfinance: An Alliance for Growth*.

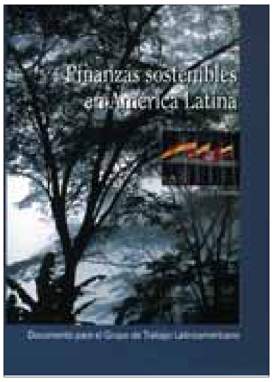
This year was also very active in dealing with environmental sustainability and the use of natural capital. CAF published four books, namely *Biotechnology for the Sustainable Use of Biodiversity: Local Capacities and Potential Market*; *Biocommerce in the Andean Subregion: Opportunities for Development*; *Sustainable Finances in Latin America*; and *Elements for the Specific Protection of Integral, Collective and Traditional Knowledge from a Native Perspective*.

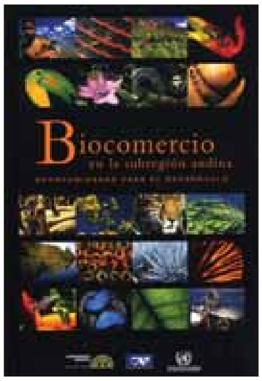
With respect to social issues, it should be noted that the series, Working Papers on Social and Educational Development, was initiated with the publication of *Books for Children and Youths. Current situation of their Production and Distribution in Andean Countries*. This project, which is part of an integral approach, stems from the need to work jointly with institutions representing the eductional sector in CAF member countries.





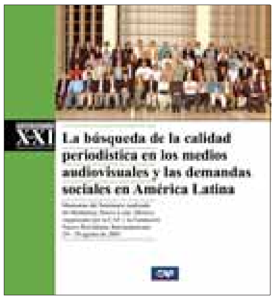


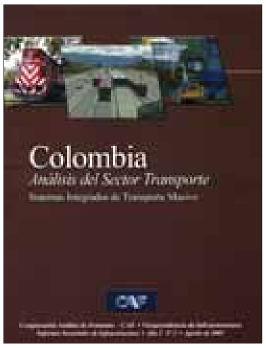



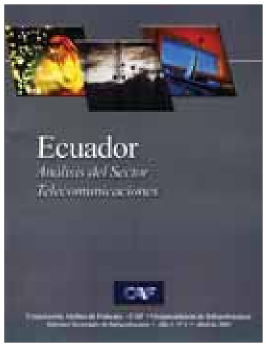





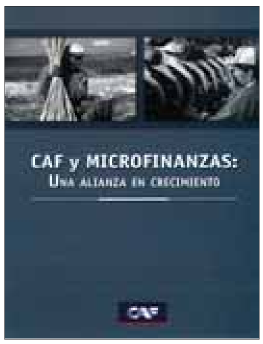




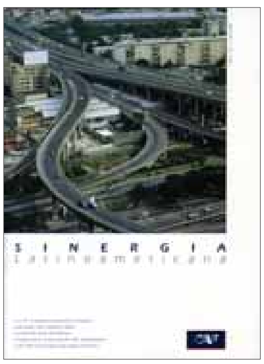



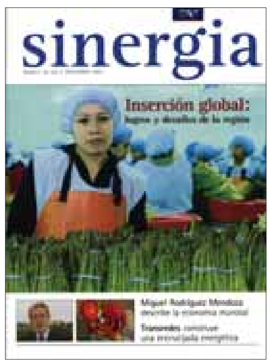

**Dissemination of knowledge**
During 2005, CAF's publications were aimed at disseminating information on crucial issues with the purpose of supporting the renewed agenda for development being implemented in Latin America, with emphasis on the areas of regional integration, infrastructure, economic competitiveness, environment, microfinance and education.

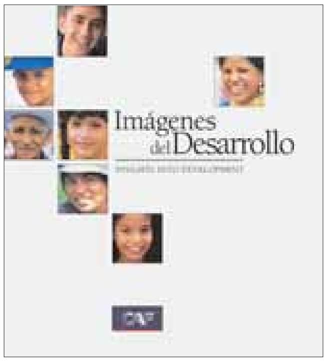














In 2005, too, two new titles of the Journalists of the 21st Century series were published. These were *The Search for Journalistic Quality and the Transformation of Professional Journalism* and *The Search for Journalistic Quality in the Audiovisual Media and Social Demands in Latin America*. Likewise, as part of its external communications efforts by way of contribution to the development of the Corporation's mission, three new editions of the *Latin American Synergy* magazine were published.

Finally, it should be emphasized that the book, *Insights into Development*, was published as part of the commemoration of the 35th Anniversary of CAF. This is a small but highly attractive book that shows the reader some of the most impressive projects that have been financed by the institution in the public and private sectors of member countries and that have been undertaken in different areas of economics and of human, social and environmental development.

Anyone wishing to access the books of the Corporation published in digital format, should kindly go to **www.caf.com/publicaciones**.

## Organizational Issues

CAF maintains a permanent program of institutional modernization and updating to fulfill the needs of its shareholders and clients in a timely and satisfactory manner. During 2005, the Corporation's organizational activities were geared toward strengthening the adjustment process of its organizational structure undertaken in 2004 to enhance its internal organization and strengthen its competitive advantages.

A new human capital management strategy was developed, in line with the Corporation's medium-term business strategies, to continue attracting, developing and retaining talented personnel with the critical skills required to ensure the achievement present and future institution goals.

In processes and technology, the Corporation continued the development of the Business Continuity Plan, delivered the Client Operation System to different business, completed the Funds Administration System and the conceptual design of the Registry Management Program. It was defined a set of guidelines, allowing the launching of a project to classify and digitalize all information of relevance to CAF.

With respect to the strengthening of credit administration and auditing processes, during 2005, emphasis was placed on activities related to the establishment of internal norms, follow-up on the conditions and quality of credit-related documentation, integral risk management, internal audit, ex post assessment of projects and prevention of asset laundering. The strengthening of the Internal Control System and the implementation of a methodology for managing CAF's norms are also noteworthy.

During the period, CAF started a Retirement Plan for its senior officials, upon approval by the Board of Directors in the first quarter. The Corporation also made strides with its planned corporate infrastructure projects, including the construction of its new representative office in La Paz, Bolivia, the purchase of land plot for its new headquarters in Caracas, Venezuela, and the expansion of its representative office in Quito, Ecuador.

As for external communications activities, CAF's presence and image were strengthened in 2005 with the communications media and targeted audiences. In addition, CAF's Web site was further restructured with the development of several theme-related subportals, such as that of the Economic Studies, the Kemmerer Program and the Information and Documentation Center (CID), and two subportals directed at investors and media professionals, respectively. In addition, CAF continued to develop its electronic portal Órganos Colegiados for the exclusive use of the members of the Board of Directors, in order to provide them with a channel for communications and timely information about institutional activities.

## As part of CAF's strategic programs, there are ten electronic subportals providing information to clients, investors and other users on its products, services and fields of action

www.caf.com/cid

www.caf.com/condor

www.caf.com/biocaf

www.caf.com/gobernabilidad

www.caf.com/plac

www.caf.com/iirsa

www.caf.com/prensa

www.caf.com/pac

www.caf.com/kemmerer

www.caf.com/cultural










# Clients, products and services

CAF, A STEADILY GROWING MULTILATERAL SOURCE of financing for its shareholder countries, provides its clients with resources to promote integration, sustainable development, trade and investment, all within a framework of efficiency, profitability and competitiveness. The Corporation raises resources in the international financial markets, and channels them into multiple, high value-added financial services, which it provides in a timely manner. CAF designs its products and services to meet its clients' requirements, and to take advantage of prevailing market opportunities.

## CAF's clients

CAF makes its products and services available to the governments of its member countries, as well as to public, private and joint ventures operating in the productive and financial sectors in these countries.

## Products and services

Briefly, CAF's principal products and services are the following:

- Short-, medium- and long-term loans.
- Structured finance and limited-recourse project finance.
- Co-financing with either multilateral or official national institutions, as well as with international banks - including A/B loans.
- Investment banking and financial advisory services.
- Guarantees.
- Equity investments.
- Treasury products
- Technical cooperation.
- Other services.

## Loans

CAF's principal line of business is lending short term (up to one year), medium term (1 to 5 years), and long term (over 5 years), to finance investment projects and other requirements of member-country governments, as well as of the public and private corporate and financial sectors. CAF also provides lines of credit to finance import and export operations, and working capital requirements.

- Project loans can be used to finance virtually any investment category in the various sectors in which the Corporation is active.
- Project finance can be made available as non-recourse or limited-recourse lending.
- Acting as second-story lender, CAF provides loans and lines of credit to public or private financial institutions that, in turn, lend the funds to end-users, such as small- and medium-size enterprises.
- The Corporation also makes loans to help develop small- and medium-size enterprises and micro-financial corporations.

## Co-financing

CAF undertakes co-financing operations to attract additional external resources to the region, thereby substantially increasing the flow of financing for public and private investment to assist its clients. CAF's partners in co-financing operations are other multilateral organizations, government agencies, and international commercial banks, the latter mostly through A/B loans.

## Investment banking and financial advisory services

CAF supports clients through investment banking operations that help add value to its traditional products and to provide comprehensive financial services. Included are consulting services for structured financial transactions, used to put together highly complex operations designed to fit each individual client's financing requirements. Financial consulting is provided in connection with concessions, privatizations and public bidding processes, as well as in the search for preferable financing options for the private sector. In certain cases CAF may also structure the transaction.

## Guarantees

CAF can provide guarantees to corporations and to financial institutions in support of credit supplied to its clients from other sources. This line of products includes partial guarantees to enhance the credit rating of bond issues and borrowings, and to assist in the establishment of structured trust funds. CAF may also underwrite the placement of fixed-income securities in the region's capital markets, thereby not only securing the required funding for its clients, but also promoting the development of such markets.

## Equity investments

CAF's equity investments are mostly in investment funds, which in turn channel resources to specific ventures. Only exceptionally will CAF consider taking a direct equity position in a given corporation or financial institution.

To assist with the special needs of small- and medium-size firms, CAF has established a Corporate Investment and Development Fund for Small- and Medium-Size Enterprises (FIDE), which is able to take equity positions in such firms, as well as to participate in the capital of investment funds and regulated financial institutions specialized in supporting such enterprises.

## Treasury products

CAF's treasury products are provided exclusively to its regional clients. Such services include the placement of regional bond issues, and the acceptance of deposits through a money desk. Operations range from very short term, such as overnight deposits, to up to three years, thereby fitting a variety of clients' needs. Fund management services are also provided by CAF in this connection.

## Technical cooperation

Using resources earmarked for this purpose, CAF funds specialized operations designed to strengthen technical capabilities in the member countries. Depending upon its particular nature and purpose, a technical assistance operation can be made reimbursable, non-reimbursable or contingent-recovery.

Technical assistance operations are channeled toward such areas as government-sponsored modernization of the state; privatization, decentralization and institutional reform; export and investment promotion; development and integration of regional capital markets; application of technology for competitiveness; environmental protection; programs for cultural and community development, and traditional art training; in short, to efforts with high social, developmental and integrationist content.

CAF has established a special program for the Andean region, the Fund for Human Development (FONDESHU), to cater to the neediest rural sectors and to promote productive community development projects that have innovative components and which have been seen to be successful. FONDESHU's resources are also used to finance selected micro-financial organizations, and to aid their institutional strengthening efforts.

## Administration of third-party funds

CAF manages and supervises the use of certain funds supplied by donor countries and agencies, most often on a non-reimbursable basis, as long as their objectives and their conditions are coherent with CAF's policies and strategies. An example of this type of arrangement is one with the International Fund for Agricultural Development (IFAD), designed to alleviate rural hunger and poverty, and to improve the living standards of the indigenous people in the region. Another is the technical cooperation fund established by the Spanish Ministry of the Economy, aimed at funding preinvestment projects in integration, institutional reform, infrastructure, energy, social development and environmental protection.

# Financial statements

# Independent Auditors' Report

The Board of Directors and Stockholders of
Corporación Andina de Fomento (CAF):

We have audited the accompanying balance sheets of Corporación Andina de Fomento (CAF) as of December 31, 2005 and 2004, and the related statements of income, stockholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Corporation's management. 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 of America. 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 also includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Corporation's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Corporación Andina de Fomento (CAF) as of December 31, 2005 and 2004, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

KPMG

January 27, 2006
Caracas, Venezuela

### Balance sheets. December 31, 2005 and 2004

(In thousands of U.S. dollars)

| Assets | Note | 2005 | 2004 |
|---|---|---|---|
| Cash and due from banks | | 1,740 | 2,753 |
| Deposits with banks | 2 | 334,571 | 369,990 |
| Marketable securities | | | |
| Trading | 3 | 1,105,568 | 1,017,716 |
| Held-to-maturity | 3 | 87,885 | 166,362 |
| Other investments | 2 | 258,576 | 170,521 |
| Loans | 4 | 7,346,978 | 7,104,123 |
| Less allowance for losses | 4 | 161,629 | 181,801 |
| Loans, net of allowance for losses | | 7,185,349 | 6,922,322 |
| Equity investments | 5 | 114,646 | 112,135 |
| Interest and commissions receivable | | 181,939 | 151,047 |
| Property and equipment | 6 | 10,986 | 12,612 |
| Other assets | 7 | 259,394 | 660,511 |
| **Total assets** | | **9,540,654** | **9,585,969** |
| | | | |
| **Liabilities and Stockholders' Equity** | | | |
| Deposits | 8 | 386,419 | 205,346 |
| Commercial paper | 9 | 710,270 | 712,406 |
| Advances and short-term borrowings | | 443,707 | 529,190 |
| Bonds | 10 | 4,061,108 | 4,574,718 |
| Borrowings and other obligations | 11 | 489,972 | 574,959 |
| Accrued interest and commissions payable | | 110,954 | 95,857 |
| Accrued expenses and other liabilities | 12 | 101,063 | 100,852 |
| **Total liabilities** | | **6,303,493** | **6,793,328** |
| Subscribed and paid-in capital (authorized capital US$5,000 million) | | 1,681,885 | 1,498,675 |
| Additional paid-in capital | | 239,524 | 220,072 |
| Reserves | | 1,032,514 | 866,141 |
| Retained earnings | | 283,238 | 207,753 |
| **Total stockholders' equity** | 14 | **3,237,161** | **2,792,641** |
| **Total liabilities and stockholders' equity** | | **9,540,654** | **9,585,969** |

See accompanying notes to the financial statements.

# Statements of income



**Statements of income. Years ended December 31, 2005 and 2004**

**(In thousands of U.S. dollars)**

| | Note | 2005 | 2004 |
|---|---|---|---|
| Interest income | | | |
| Loans | 1(f) | 462,716 | 327,363 |
| Investments and deposits with banks | 1(e) | 59,433 | 27,992 |
| Loan commissions | 1(f) | 25,423 | 23,352 |
| **Total interest income** | | **547,572** | **378,707** |
| | | | |
| Interest expense | | | |
| Deposits | | 12,319 | 3,359 |
| Commercial paper | | 15,789 | 8,852 |
| Advances and short-term borrowings | | 12,986 | 8,250 |
| Bonds | | 188,551 | 123,919 |
| Borrowings and other obligations | | 21,069 | 11,392 |
| Commissions | | 4,871 | 5,094 |
| **Total interest expense** | | **255,585** | **160,866** |
| | | | |
| Net interest income | | 291,987 | 217,841 |
| Credit to allowance for loan losses | 4 | (14,500) | (18,555) |
| | | | |
| Net interest income, after credit for loan losses | | 306,487 | 236,396 |
| Non-interest income | | | |
| Other commissions | | 5,814 | 2,548 |
| Dividends and equity in earnings of investees | | 13,358 | 8,137 |
| Other income | | 1,721 | 1,542 |
| **Total non-interest income** | | **20,893** | **12,227** |
| Non-interest expenses | | | |
| Administrative expenses | | 42,640 | 38,120 |
| Impairment charge for equity investments | 5 | 24 | 1,694 |
| Inecffectiveness arising from fair value hedges | | 1,146 | 828 |
| Other expenses | | 332 | 228 |
| **Total non-interest expenses** | | **44,142** | **40,870** |
| | | | |
| **Net income** | | **283,238** | **207,753** |

See accompanying notes to the financial statements.

# Statements of stockholders' equity

Corporación Andina de Fomento

**Annual Report 2005**

**Statements of stockholders' equity. Years ended December 31, 2005 and 2004**

**(In thousands of U.S. dollars)**

| | Note | Subscribed and paid-in capital | Additional paid-in capital | Reserve pursuant to General reserve | Reserve pursuant to Article No. 42 of by-laws | Total reserves | Retained earnings | Total stock-holders' equity |
|---|---|---|---|---|---|---|---|---|
| **Balances at December 31, 2003** | | **1,318,555** | **173,460** | **560,088** | **192,520** | **752,608** | **135,533** | **2,380,156** |
| Capital increase | 14 | 106,915 | 119,817 | - | - | - | - | 226,732 |
| Stock dividends | 14 | 73,205 | (73,205) | - | - | - | - | - |
| Net income | 14 | - | - | - | - | - | 207,753 | 207,753 |
| Appropriated for general reserve | 14 | - | - | 99,979 | - | 99,979 | (99,979) | - |
| Appropriated for reserve pursuant to Article No. 42 of by-laws | 14 | - | - | - | 13,554 | 13,554 | (13,554) | - |
| Allocations to stockholders' funds | 15 | - | - | - | - | - | (22,000) | (22,000) |
| **Balances at December 31, 2004** | | **1,498,675** | **220,072** | **660,067** | **206,074** | **866,141** | **207,753** | **2,792,641** |
| Capital increase | 14 | 95,110 | 107,552 | - | - | - | - | 202,662 |
| Stock dividends | 14 | 88,100 | (88,100) | - | - | - | - | - |
| Net income | 14 | - | - | - | - | - | 283,238 | 283,238 |
| Appropriated for general reserve | 14 | - | - | 145,573 | - | 145,573 | (145,573) | - |
| Appropriated for reserve pursuant to Article No. 42 of by-laws | 14 | - | - | - | 20,800 | 20,800 | (20,800) | - |
| Allocations to stockholders' funds | 15 | - | - | - | - | - | (41,380) | (41,380) |
| **Balances at December 31, 2005** | | **1,681,885** | **239,524** | **805,640** | **226,874** | **1,032,514** | **283,238** | **3,237,161** |

See accompanying notes to the financial statements.

# Statements of cash flows

Corporación Andina de Fomento
**Annual Report 2005**

**Statements of cash flows. Years ended December 31, 2005 and 2004**

**(In thousands of U.S. dollars)**

| | Note | 2005 | 2004 |
|---|---|---|---|
| Cash flows from operating activities - | | | |
| Net income | | 283,238 | 207,753 |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities - | | | |
| Credit to allowance loan losses | 4 | (14,500) | (18,555) |
| Impairment charge for equity investments | 5 | 24 | 1,694 |
| Equity in earnings of investees | | (8,273) | (6,138) |
| Amortization of deferred charges | | 3,138 | 2,764 |
| Depreciation of property and equipment | 6 | 3,115 | 2,735 |
| Loss on sale of property and equipment | | 37 | - |
| Provision for employees' severance indemnities and benefits | | 4,544 | 3,775 |
| Provision for employees' savings plan | | 1,497 | 1,464 |
| Net changes in operating assets and liabilities | | | |
| Securities purchased under resale agreements | | - | 25,000 |
| Net loss (gain) on sale of trading securities | 3 | (56) | 2,019 |
| Severance indemnities paid or advanced | | (2,863) | (1,875) |
| Employees' savings plan paid or advanced | | (1,532) | (559) |
| Trading securities | 3 | (87,796) | (381,876) |
| Interest and commissions receivable | | (30,892) | (15,846) |
| Other assets | | (12,819) | 20,449 |
| Accrued interest and commissions payable | | 15,097 | (2,320) |
| Accrued expenses and other liabilities | | (3,070) | (5,666) |
| **Total adjustments and net changes in operating assets and liabilities** | | **(134,349)** | **(372,935)** |
| | | | |
| **Net cash provided by (used in) operating activities** | | **(148,889)** | **(165,182)** |
| | | | |
| Cash flows from investing activities | | | |
| Purchases of held-to-maturity securities | 3 | (732,383) | (471,688) |
| Maturities of held-to-maturity securities | 3 | 810,860 | 622,330 |
| Other investments | 2 | (88,055) | (75,015) |
| Loan origination and principal collections, net | 4 | (246,510) | (521,984) |
| Equity investments | 5 | 5,738 | 7,336 |
| Purchases of property and equipment | 6 | (1,489) | (5,016) |
| **Net cash used in investing activities** | | **(251,839)** | **(444,037)** |
| | | | |
| **Carried forward** | | **(102,950)** | **(609,219)** |

## Statements of cash flows. Years ended December 31, 2005 and 2004

**(In thousands of U.S. dollars)**

| | Note | 2005 | 2004 |
|---|---|---|---|
| **Brought forward** | | **(102,950)** | **(609,219)** |
| | | | |
| Cash flows from financing activities - | | | |
| Net (decrease) increase in deposits | | 181,073 | (72,826) |
| Net increase in commercial paper | | 3,213 | 35,790 |
| Net (decrease) increase in advances and short-term borrowings | | (59,254) | 36,976 |
| Proceeds from issuance of bonds | 10 | 584,332 | 657,500 |
| Repayment of bonds | 10 | (724,624) | (644,534) |
| Proceeds from borrowings and other obligations | 11 | 20,000 | 244,166 |
| Repayment of borrowings and other obligations | 11 | (99,504) | (87,531) |
| Allocations to stockholders' funds | 15 | (41,380) | (22,000) |
| Proceeds from issuance of shares | 14 | 202,662 | 226,732 |
| **Net cash provided by financing activities** | | **66,518** | **374,273** |
| | | | |
| Net decrease in cash and cash equivalents | | (36,432) | (234,946) |
| | | | |
| Cash and cash equivalents at beginning of year | | 372,743 | 607,689 |
| **Cash and cash equivalents at end of year** | | **336,311** | **372,743** |
| | | | |
| Consisting of : | | | |
| Cash and due from banks | | 1,740 | 2,753 |
| Deposits with banks | | 334,571 | 369,990 |
| | | 336,311 | 372,743 |
| Supplemental disclosure - | | | |
| Interest paid during the year | | 235,717 | 157,993 |
| | | | |
| Noncash financing activities - | | | |
| Change in other assets due to fair value hedging relationships | | (410,761) | 196,372 |
| Change in other liabilities due to fair value hedging relationships | | 2,781 | (107,688) |

See accompanying notes to the financial statements.

# (1) Significant Accounting Policies

## (a) Description of Business

Corporación Andina de Fomento ("CAF" or the "Corporation") commenced operations on June 8, 1970 and is a corporation under public international law which abides by the provisions of its by-laws. Shareholder countries are: Bolivia, Colombia, Ecuador, Peru and Venezuela, members of the Andean Community Nations, together with Argentina, Brazil, Chile, Costa Rica, Jamaica, Mexico, Paraguay, Panama, Spain, Trinidad and Tobago and Uruguay, in addition to 16 banks of the region. The Corporation has its headquarters in Caracas, Venezuela.

The Corporation's principal activity is to provide short, medium and long-term loans to finance projects, working capital, trade activities and to undertake feasibility studies for investment opportunities in its member countries.

## (b) Financial Statements Presentation

The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America and the functional currency is the U.S. dollar.

In preparing financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Certain amounts in the prior year have been reclassified to conform to the current year's presentation.

## (c) Foreign Currency Transactions

Transactions in currencies other than U.S. dollars are translated at exchange rates prevailing on the international market at the dates of the transactions. Foreign currency balances are translated at year-end exchange rates. Any gains or losses on foreign exchange including related hedge effects are included the statement of income and are not significant.

## (d) Cash Equivalents

Cash equivalents are defined as cash, due from banks and deposits with banks.

## (e) Marketable Securities

Marketable securities at December 31, 2005 and 2004 consist of U.S. Treasury and debt securities.

The Corporation classifies its debt securities in one of two categories: trading or held-to-maturity. Trading securities are bought and held principally for the purpose of selling them in the near term. Held-to-maturity securities are those securities which the Corporation has the ability and intent to hold until maturity.

Trading securities are recorded at fair value. Unrealized gains and losses on trading securities are included in earnings.

Held-to-maturity securities are recorded at amortized cost, adjusted for the amortization or accretion of premiums or discounts. A decline in the market value of any held-to-maturity security below cost that is deemed to be other than temporary results in a reduction in carrying amount. The impairment is charged to income and a new cost basis for the security is established. Premiums and discounts are amortized or accreted over the life of the related held-to-maturity security as an adjustment to yield using the effective interest method.

Dividend and interest income are recognized when received and earned, respectively.

## (f) Loans

The Corporation grants short, medium and long-term loans to finance projects, working capital, trade activities and undertake feasibility studies for investment opportunities in its member countries. Loans are reported at their outstanding unpaid principal balances adjusted for charge-offs, less the allowance for loan losses. Interest income is accrued on the unpaid principal balance. Loan commission fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using the interest method and are presented as loan commissions in the statement of income.

The accrual of interest on loans is discontinued at the time a private sector loan is 90 days (180 days for public sector loans) delinquent unless the credit is well-secured and in process of collection.

All interest accrued but not collected for loans that are placed on nonaccrual or charged off is reversed against interest income. The interest on these loans is accounted for on the cash-basis, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

The nonaccrual loans are considered impaired. Factors considered by management in determining impairment include payments status, collateral value, and the probability of collecting scheduled principal and interest payments when due.

## (g) Equity Investments

CAF participates with equity investments in companies and investment funds in strategic sectors, with a view to promoting the development of such companies in shareholder countries and their participation in the securities markets and to serve as a catalytic agent in attracting resources into the region.

Equity investments are accounted for using the equity method or at cost. If the Corporation has the ability to exercise significant influence over the operating and financial policies of the investee, which is generally presumed to exist at a 20% of equity ownership level, the equity investments are accounted for using the equity method. Under the equity method, the carrying value of the equity investment is adjusted for its proportionate share of earnings or losses, dividends received and certain other transactions of the investee company.

A decline in the market value of any equity investment accounted for at cost, that is deemed to be other than temporary, results in a reduction in carrying amount to fair value. The impairment is charged to income and a new cost basis for the investment is established.

## (h) Allowance for Loan Losses

The allowance for loan losses is maintained at a level the Corporation believes is adequate but not excessive to absorb probable losses inherent in the loan portfolio as of the date of the financial statements. The general allowance for loan losses is established by the Corporation based on the individual risk rating for the long term foreign currency debt of the borrower countries which is assigned by the international risk rating agencies as of the date of the financial statements preparation. This country risk rating considers a default probability. In the case of sovereign loan portfolio a factor of preferred creditor status is also considered.

A specific allowance is established by the Corporation for those loans that are considered impaired. A loan is considered as impaired when based on currently available information and events, there exists the probability that CAF will not recover the total amount of principal and interest as agreed in the terms of the original loan contract. The impairment of loans is determined on a loan by loan basis based on the present value of expected future cash flows, discounted at the loans effective interest rate.

Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

## (i) Property and Equipment

Property and equipment are stated at cost less accumulated depreciation. Depreciation, calculated on the straight-line method, is charged to operations over the estimated useful lives of assets.

## (j) Employees' Severance Indemnities

The Corporation accrues for employees' severance indemnities in accordance with the Corporation's personnel regulations and the Partial Reform of the Organic Labor Law of the Bolivarian Republic of Venezuela, which establish that employees are entitled to an indemnity upon the termination of employment, equivalent to five days remuneration for each month of service, plus two days for each year of service up to a maximum of 30 days, commencing from the second year. Under certain circumstances the reformed law also provides for the payment for unjustified dismissal. The accrual is presented net of advances and interest is paid annually on the outstanding balance.

## (k) Pension Plan

The Corporation established in March 2005 a defined benefit pension plan (the Plan). The Plan is contributory and the benefits are based on years of service and the average employee's salary for the three consecutive years of service with the highest salary.

## (l) Derivative Instruments and Hedging Activities

All derivatives are recognized on the balance sheet at their fair value. On the date the derivative contract is entered into, the Corporation designates the derivative as either a hedge of the fair value of a recognized asset or liability or of an unrecognized firm commitment ("fair value" hedge), a hedge of a forecasted transaction or the variability of cash flows to be received or paid related to a recognized asset or liability ("cash flow" hedge), or a foreign-currency fair-value or cash-flow hedge ("foreign currency" hedge). The Corporation formally documents all relationships between hedging instruments and hedged items, as well as its risk-management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives that are designated as fair-value, cash-flow, or foreign-currency hedges to specific assets and liabilities on the balance sheet or to specific firm commitments or forecasted transactions. The Corporation also formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. When it is determined that a derivative is not highly effective as a hedge or that it has ceased to be a highly effective hedge, the Corporation discontinues hedge accounting prospectively.

Changes in the fair value of a derivative that is highly effective and that is designated and qualifies as a fair-value hedge, along with the loss or gain on the hedged asset or liability or unrecognized firm commitment of the hedged item that is attributable to the hedged risk, are recorded in income. Changes in the fair value of a derivative that is highly effective and that is designated and qualifies as a cash-flow hedge are recorded in other comprehensive income, until income is affected by the variability in cash flows of the designated hedged item. Changes in the fair value of derivatives that are highly effective as hedges and that are designated and qualify as foreign-currency hedges are recorded in either income or other comprehensive income, depending on whether the hedge transaction is a fair-value hedge or a cash-flow hedge.

The Corporation discontinues hedge accounting prospectively when it is determined that the derivative is no longer effective in offsetting changes in the fair value or cash flows of the hedged item, the derivative expires or is sold, terminated, or exercised, the derivative is de-designated as a hedging instrument, because it is unlikely that a forecasted transaction will occur, a hedged firm commitment no longer meets the definition of a firm commitment, or management determines that designation of the derivative as a hedging instrument is no longer appropriate.

When hedge accounting is discontinued because it is determined that the derivative no longer qualifies as an effective fair-value hedge, the Corporation continues to carry the derivative on the balance sheet at its fair value, and no longer adjusts the hedged asset or liability for changes in fair value. The adjustment of the carrying amount of the hedged asset or liability is accounted for in the same manner as other components of the carrying amount of that asset or liability. When hedge accounting is discontinued because the hedged item no longer meets the definition of a firm commitment, the Corporation continues to carry the derivative on the balance sheet at its fair value, removes any asset or liability that was recorded pursuant to recognition of the firm commitment from the balance sheet and recognizes any gain or loss in income. When hedge accounting is discontinued because it is probable that a forecasted transaction will not occur, the Corporation continues to carry the derivative on the balance sheet at its fair value, and gains and losses that were accumulated in other comprehensive income are recognized immediately in income. In all other situations in which hedge accounting is discontinued, the Corporation continues to carry the derivative at its fair value on the balance sheet, and recognizes any changes in its fair value in income.

## (2) Deposits with Banks and Other Investments

Deposits with banks mature in three months or less and include the following:

(In thousands of U.S. dollars)

| | December 31, | |
|---|---|---|
| | **2005** | **2004** |
| U.S. dollars | 331,098 | 363,564 |
| Other currencies | 3,473 | 6,426 |
| | **334,571** | **369,990** |

Deposits with maturities over 90 days are reported in the balance sheets as other investments.

## (3) Marketable Securities

### Trading Securities

A summary of trading securities follows:

(In thousands of U.S. dollars)

| | **Amount** | **Average maturity (years)** | **Average yield%** |
|---|---|---|---|
| **At December 31, 2005 -** | | | |
| U. S. Treasury Notes | 39,762 | 0.37 | 3.56 |
| Bonds of non-U.S. governments and government entities | 237,616 | 1.47 | 3.66 |
| Financial institutions and corporate securities | 828,190 | 1.83 | 4.04 |
| | **1,105,568** | **1.70** | **3.94** |
| **At December 31, 2004 -** | | | |
| U. S. Treasury Notes | 48,837 | 0.69 | 2.14 |
| Bonds of non-U.S. governments and government entities | 269,021 | 1.86 | 1.66 |
| Financial institutions and corporate securities | 699,858 | 1.80 | 2.47 |
| | **1,017,716** | **1.76** | **2.24** |

Trading securities include net unrealized gains of US$332 and US$391 at December 31, 2005 and 2004, respectively.

## Held-to-Maturity Securities

A summary of held-to-maturity securities follows:

(In thousands of U.S. dollars)

| | Amortized cost | Gross unrealized holding gains | Gross unrealized holding losses | Fair value |
|---|---|---|---|---|
| **At December 31, 2005 -** | | | | |
| U. S. Treasury Notes | 5,001 | - | (21) | 4,980 |
| Bonds of non-U.S. governments and government entities | 37,884 | 5 | (21) | 37,868 |
| Financial institutions and corporate securities | 45,000 | - | - | 45,000 |
| | **87,885** | **5** | **(42)** | **87,848** |
| **At December 31, 2004 -** | | | | |
| U. S. Treasury Notes | 5,008 | - | (75) | 4,933 |
| Bonds of non-U.S. governments and government entities | 109,852 | 50 | (100) | 109,802 |
| Financial institutions and corporate securities | 51,502 | - | (4) | 51,498 |
| | **166,362** | **50** | **(179)** | **166,233** |

Held-to-maturity securities mature as follows:

(In thousands of U.S. dollars)

| | December 31, 2005 | December 31, 2004 |
|---|---|---|
| **Remaining Maturities -** | | |
| Less than one year | 80,373 | 96,712 |
| Between one and two years | 7,512 | 53,000 |
| Between two and three years | - | 10,000 |
| Between three and four years | - | 6,650 |
| Between four and five years | - | - |
| | **87,885** | **166,362** |

## (4) Loans

Loans include short, medium and long-term loans to finance projects, working capital and trade activities. The majority of the loan contracts have been subscribed with the members of the Andean Community or with private institutions or companies of these countries.

Loans by country are summarized as follows:

(In thousands of U.S. dollars)

| | Bolivia | Colombia | Ecuador | Peru | Venezuela | Other | Total |
|---|---|---|---|---|---|---|---|
| **At December 31, 2005 -** | | | | | | | |
| Loans | 981,643 | 1,899,517 | 1,230,543 | 1,712,262 | 1,134,678 | 387,995 | 7,346,638 |
| Fair value adjustments on hedging activities | | | | | | | 340 |
| Carrying value of loans | | | | | | | **7,346,978** |
| | | | | | | | |
| **At December 31, 2004 -** | | | | | | | |
| Loans | 929,211 | 1,701,891 | 1,224,217 | 1,649,817 | 1,197,048 | 403,616 | 7,105,800 |
| Fair value adjustments on hedging activities | | | | | | | (1,677) |
| Carrying value of loans | | | | | | | **7,104,123** |

Fair value adjustments to the carrying value of loans represent adjustments to the carrying value of transactions in designated fair value hedging relationships.

At December 31, 2004, loans in other currencies were granted for an equivalent of US$ 253, principally in euro and yen. At December 31, 2005 and 2004, loans include fixed interest rate loans of US$ 104,052 and US$ 226,455, respectively.

The loan portfolio composition and average yield of loans disbursed and outstanding are summarized below:

(In thousands of U.S. dollars)

| | December 31, | | | |
|---|---|---|---|---|
| | **2005** | | **2004** | |
| | **Amount** | **Average yield (%)** | **Amount** | **Average yield (%)** |
| Loans | 7,346,638 | 7.42 | 7,105,800 | 5.58 |

Loans by industry segments are as follows:

(In thousands of U.S. dollars)

| | December 31, | | | |
|---|---|---|---|---|
| | **2005** | **%** | **2004** | **%** |
| Agriculture, hunting and forestry | 220,279 | 3 | 264,402 | 4 |
| Exploitation of mines and quarries | 10,000 | 1 | 13,493 | 1 |
| Manufacturing industry | 168,633 | 2 | 162,571 | 2 |
| Supply of electricity, gas and water | 838,646 | 11 | 820,044 | 12 |
| Transport, warehousing and communications | 2,751,072 | 37 | 2,770,014 | 38 |
| Commercial banks | 492,515 | 7 | 373,934 | 5 |
| Development banks | 252,742 | 3 | 344,194 | 5 |
| Social and other infrastructure programs | 2,582,288 | 35 | 2,313,430 | 32 |
| Other activities | 30,463 | 1 | 43,718 | 1 |
| | **7,346,638** | **100** | **7,105,800** | **100** |

Loans mature as follows:

(In thousands of U.S. dollars)

| | December 31, | |
|---|---|---|
| | **2005** | **2004** |
| **Remaining maturities -** | | |
| Less than one year | 1,374,268 | 1,220,458 |
| Between one and two years | 996,721 | 1,075,125 |
| Between two and three years | 910,545 | 945,027 |
| Between three and four years | 764,184 | 830,100 |
| Between four and five years | 722,714 | 653,946 |
| Over five years | 2,578,206 | 2,381,144 |
| | **7,346,638** | **7,105,800** |

At December 31, 2005 and 2004, all loans were performing except for certain loans which were classified as impaired and were in nonaccrual status. At December 31, 2005 and 2004, the carrying value of impaired loans was approximately US$ 1,332 and US$ 19,958, respectively. The average recorded investment in impaired loans during the years ended December 31, 2005 and 2004 was approximately US$ 9,331 and US$ 14,598, respectively.

Had these loans not been in impairment status, income for the years ended December 31, 2005 and 2004 would have increased by US$ 577 and US$ 901, respectively. During the year ended December 31, 2005, there were interest collections against impaired loans amounting to US$ 76.

### Loan Participations and A/B Loans

The Corporation administers loan participations provided to clients, and assumes the credit risk only for that portion of the loan corresponding to the Corporation. During 2005 and 2004, the Corporation administered loans of this nature whereby other financial institutions provided funds amounting to US$ 441,221 and US$ 112,500, respectively.

### Allowance for Loan Losses

Movements of the allowance for loan losses follow:

(In thousands of U.S. dollars)

| | December 31, | |
|---|---|---|
| | **2005** | **2004** |
| **Balances at beginning of year** | **181,801** | **209,766** |
| Provision credited to results of operations | (14,500) | (18,555) |
| Recoveries | 4,696 | 3,522 |
| Loans charged off | (10,368) | (12,932) |
| **Balances at end of year** | **161,629** | **181,801** |

## (5) Equity Investments

A summary of equity investments follows:

(In thousands of U.S. dollars)

| | December 31, | |
|---|---|---|
| | **2005** | **2004** |
| **Direct investments in companies** (including investments accounted for using the equity method of US$ 5,456 and US$ 5,357, at December 31, 2005 and 2004, respectively) | 10,640 | 11,277 |
| **Investment funds** (including investments accounted for using the equity method of US$ 72,826 and US$ 69,543, at December 31, 2005 and 2004, respectively) | 104,006 | 100,858 |
| | **114,646** | **112,135** |

The Corporation recorded an impairment charge of US$ 24 and US$ 1,694 for the years ended December 31, 2005 and 2004, respectively, related to equity investments accounted for at cost.

## (6) Property and Equipment

A summary of property and equipment follows:

(In thousands of U.S. dollars)

| | December 31, 2005 | December 31, 2004 |
|---|---|---|
| Buildings | 20,149 | 20,149 |
| Buildings improvements | 10,035 | 9,550 |
| Furniture and equipment | 6,323 | 5,393 |
| Vehicles | 328 | 363 |
| | 36,835 | 35,455 |
| Less accumulated depreciation | 25,849 | 22,843 |
| | **10,986** | **12,612** |

Depreciation is provided for property and equipment on the straight-line method over the estimated useful lives of the respective classes of assets, as follows:

| | |
|---|---|
| Buildings | 15 years |
| Buildings improvements | 5 years |
| Furniture and equipment | 2 to 5 years |
| Vehicles | 5 years |

## (7) Other Assets

A summary of other assets follows:

(In thousands of U.S. dollars)

| | December 31, 2005 | December 31, 2004 |
|---|---|---|
| Deferred charges | 36,629 | 25,681 |
| Derivative assets (see note 17) | 215,320 | 626,081 |
| Other assets | 7,445 | 8,749 |
| | **259,394** | **660,511** |

## (8) Deposits

The Corporation's deposits of US$ 386,419 at December 31, 2005 mature in 2006 (US$ 205,346 at December 31, 2004 - mature in 2005).

## (9) Commercial Paper

The Corporation's commercial paper of US$ 710,270 at December 31, 2005 matures in 2006 (US$ 712,406 at December 31, 2004 - matures in 2005). At December 31, 2005 and 2004, the interest rates on commercial paper ranged from 4.23% to 4.60% and from 2.14% to 2.46%, respectively.

## (10) Bonds

An analysis of bonds follows:

(In thousands of U.S. dollars)

| | December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2005 | | | 2004 | | |
| | Principal outstanding | | Weighted average cost, after swaps (%) | Principal outstanding | | Weighted average cost, after swaps (%) |
| | At original exchange rate | At spot exchange rate | | At original exchange rate | At spot exchange rate | |
| U.S. dollars | 2,451,128 | 2,451,128 | 5.31 | 2,602,640 | 2,602,640 | 3.59 |
| Yen | 385,945 | 382,231 | 4.49 | 201,613 | 240,755 | 2.85 |
| Colombian Pesos | 100,000 | 119,003 | 4.65 | 100,000 | 113,425 | 2.84 |
| Pounds Sterling | 272,193 | 300,982 | 7.23 | 272,055 | 336,054 | 5.24 |
| Euros | 637,668 | 731,227 | 5.61 | 810,917 | 1,115,692 | 3.61 |
| | **3,846,934** | **3,984,571** | | **3,987,225** | **4,408,566** | |
| Fair value adjustments on hedging activities | | 76,537 | | | 166,152 | |
| Carrying value of bonds | | **4,061,108** | | | **4,574,718** | |

Fair value adjustments to the carrying value of bonds represent adjustments to the carrying value of transactions in designated fair value hedging relationships.

A summary of the bonds issued, by remaining maturities, follows:

(In thousands of U.S. dollars)

| | December 31, 2005 | December 31, 2004 |
|---|---|---|
| **Remaining maturities -** | | |
| Less than one year | 294,379 | 723,674 |
| Between one and two years | 499,655 | 294,484 |
| Between two and three years | 287,704 | 499,329 |
| Between three and four years | 584,770 | - |
| Between four and five years | 371,948 | 584,870 |
| Over five years | 1,808,478 | 1,884,868 |
| | **3,846,934** | **3,987,225** |

At December 31, 2005 and 2004, fixed interest rate bonds amounted to US$ 3,003,082 and US$ 3,090,175, respectively, of which US$ 1,117,357 and US$ 1,106,286, respectively, are denominated in yen, pounds sterling, Colombian pesos and euros.

## (11) Borrowings and Other Obligations

An analysis of borrowings and other obligations and their weighted average cost, follows:

(In thousands of U.S. dollars)

| | December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2005 | | | 2004 | | |
| | Principal outstanding | | Weighted average cost, after swaps (%) | Principal outstanding | | Weighted average cost, after swaps (%) |
| | At original exchange rate | At spot exchange rate | | At original exchange rate | At spot exchange rate | |
| U.S. dollars | 463,245 | 463,245 | 4.84 | 530,835 | 530,835 | 2.86 |
| Yen | 19,610 | 21,235 | 4.17 | 27,455 | 33,706 | 2.99 |
| Euros (at spot rate) | 3,574 | 3,574 | 5.81 | 7,613 | 7,613 | 6.40 |
| Other currencies (at spot rate) | 1,932 | 1,932 | - | 1,962 | 1,962 | - |
| | **488,361** | **489,986** | | **567,865** | **574,116** | |
| Fair value adjustments on hedging activities | | (14) | | | 843 | |
| Carrying value of borrowings and other obligations | | **489,972** | | | **574,959** | |

Fair value adjustments to the carrying value of borrowings and other obligations represent adjustments to the carrying value of transactions in designated fair value hedging relationships.

At December 31, 2005 and 2004, there are fixed interest-bearing borrowings and other obligations amounting to US$ 20,945 and US$ 27,836, respectively.

Borrowings and other obligations, by remaining maturities, are summarized below:

(In thousands of U.S. dollars)

| | December 31, | |
|---|---|---|
| | 2005 | 2004 |
| **Remaining maturities -** | | |
| Less than one year | 76,839 | 99,028 |
| Between one and two years | 110,006 | 79,266 |
| Between two and three years | 55,133 | 98,040 |
| Between three and four years | 143,890 | 50,210 |
| Between four and five years | 29,496 | 89,386 |
| Over five years | 72,997 | 151,935 |
| | **488,361** | **567,865** |

Some borrowing agreements contain covenants conditioning the use of the funds for specific purposes or projects.

At December 31, 2005 and 2004 there were unused term credit facilities amounting to US$ 128,000 and US$ 80,000, respectively.

## (12) Accrued Expenses and Other Liabilities

A summary of accrued expenses and other liabilities follows:

(In thousands of U.S. dollars)

| | December 31, | |
|---|---|---|
| | **2005** | **2004** |
| Employees' severance indemnities, benefits and savings plan | 34,346 | 32,182 |
| Derivative liabilities (see note 17) | 2,781 | - |
| Deferred income (including US$ 58,325 in 2005 and US$ 55,159 in 2004 of loan commissions, net of certain direct origination costs) | 61,184 | 64,857 |
| Other liabilities | 2,752 | 3,813 |
| | **101,063** | **100,852** |

## (13) Pension Plan

The Corporation established in March 2005 a defined benefit pension plan (the Plan) which is mandatory for all new employees as of the date of implementation of the Plan and voluntary for all other employees. The Plan is contributory and the benefits are based on years of service and the average employee's salary for the three consecutive years of service with the highest salary. The employees make monthly contributions to the Plan equal to 7% of their salary. Voluntary participants must contribute to the Plan certain withheld benefits. The Plan has 14 participants.

The measurement date used to determine pension benefit measures for the Plan is December 31.

The Plan's benefit obligation and assets as of December 31, 2005 amount to US $ 644 and US $ 639, respectively.

Weighted-average assumptions used to determine net benefit cost from the origination of the Plan to December 31, 2005 follow:

| | |
|---|---|
| Discount rate | 4 % |
| Expected long-term rate of return on Plan assets | 4 % |
| Rate of salary increase | 3 % |

## (14) Stockholders' Equity

### Authorized Capital

The authorized capital of the Corporation at December 31, 2005 and 2004, amounts to US$ 5,000,000, distributed among Series "A", "B" and "C" shares.

### Subscribed Callable Capital

The payment of subscribed callable capital will be as required, with prior approval of the Board of Directors, in order to meet financial obligations of the Corporation, when internal resources are inadequate.

### Shares

The Corporation's shares are classified as follows:

**Series "A" shares**: Subscribed by the governments or public-sector institutions, semipublic or private entities with social or public objectives of the five Andean Community member countries: Bolivia, Colombia, Ecuador, Peru and Venezuela. These shares grant the right of representation on the Corporation's board of one principal director and one alternate director per share. Series "A" shares have a par value of US$ 1,200.

**Series "B" shares**: Subscribed by the governments or public-sector institutions, semipublic or private entities and commercial banks of the five Andean Community member countries. These shares grant the right of representation on the Corporation's board of one principal director and one alternate director. Also, the commercial banks are entitled to one principal director and one alternate director on the board. Series "B" shares have a par value of US$ 5.

**Series "C" shares**: Subscribed by legal entities or individuals outside of the region. These shares provide for representation on the board of directors of the Corporation of two principal directors and their respective alternates, who are elected by the holders of these shares. Series "C" shares have a par value of US$ 5.

A summary of the movement in subscribed and paid-in capital for the years ended December 31, 2005 and 2004, follows:

(In thousands of U.S. dollars)

| | Number of Shares | | | Amounts | | | |
|---|---|---|---|---|---|---|---|
| | Series "A" | Series "B" | Series "C" | Serie s"A" | Series "B" | Series "C" | Total |
| **At December 31, 2003** | 5 | 241,505 | 21,006 | 6,000 | 1,207,525 | 105,030 | 1,318,555 |
| Dividends in shares | - | 13,478 | 1,163 | - | 67,390 | 5,815 | 73,205 |
| Issued for cash | - | 14,739 | 6,644 | - | 73,695 | 33,220 | 106,915 |
| **At December 31, 2004** | 5 | 269,722 | 28,813 | 6,000 | 1,348,610 | 144,065 | 1,498,675 |
| Dividends in shares | - | 15,931 | 1,689 | - | 79,655 | 8,455 | 88,100 |
| Issued for cash | - | 14,926 | 4,096 | - | 74,630 | 20,480 | 95,110 |
| **At December 31, 2005** | **5** | **300,579** | **34,598** | **6,000** | **1,502,895** | **172,990** | **1,681,885** |

Subscribed and paid-in capital is held as follows at December 31, 2005:

(In thousands of U.S. dollars)

| | Number of Shares | | | Amounts | | | |
|---|---|---|---|---|---|---|---|
| Stockholder | Series "A" | Series "B" | Series "C" | Series "A" | Series "B" | Series "C" | Total |
| Bolivia | 1 | 22,911 | - | 1,200 | 114,555 | - | 115,755 |
| Colombia | 1 | 83,275 | - | 1,200 | 416,375 | - | 417,575 |
| Ecuador | 1 | 24,050 | - | 1,200 | 120,250 | - | 121,450 |
| Peru | 1 | 85,047 | - | 1,200 | 425,235 | - | 426,435 |
| Venezuela | 1 | 85,047 | - | 1,200 | 425,235 | - | 426,435 |
| Argentina | - | - | 2,687 | - | - | 13,435 | 13,435 |
| Brazil | - | - | 11,297 | - | - | 56,485 | 56,485 |
| Chile | - | - | 294 | - | - | 1,470 | 1,470 |
| Costa Rica | - | - | 2,204 | - | - | 11,020 | 11,020 |
| Jamaica | - | - | 124 | - | - | 620 | 620 |
| Mexico | - | - | 3,158 | - | - | 15,790 | 15,790 |
| Panama | - | - | 1,416 | - | - | 7,080 | 7,080 |
| Paraguay | - | - | 1,224 | - | - | 6,120 | 6,120 |
| Spain | - | - | 10,455 | - | - | 52,275 | 52,275 |
| Trinidad & Tobago | - | - | 140 | - | - | 700 | 700 |
| Uruguay | - | - | 1,599 | - | - | 7,995 | 7,995 |
| Commercial banks | - | 249 | - | - | 1,245 | - | 1,245 |
| | **5** | **300,579** | **34,598** | **6,000** | **1,502,895** | **172,990** | **1,681,885** |

At December 31, 2005, the distribution of unpaid subscribed capital and of subscribed callable capital is presented below:

(In thousands of U.S. dollars)

| | Unpaid Subscribed Capital | | | | Subscribed Callable Capital | | | |
|---|---|---|---|---|---|---|---|---|
| | Series "B" | | Series "C" | | Series "B" | | Series "C" | |
| Stockholder | Number of shares | Amount | Number of shares | Amount | Number of shares | Amount | Number of shares | Amount |
| Bolivia | 2,311 | 11,555 | - | - | 14,400 | 72,000 | - | - |
| Colombia | 5,938 | 29,690 | - | - | 50,400 | 252,000 | - | - |
| Ecuador | 1,234 | 6,170 | - | - | 14,400 | 72,000 | - | - |
| Peru | 4,336 | 21,680 | - | - | 50,400 | 252,000 | - | - |
| Venezuela | 4,336 | 21,680 | - | - | 50,400 | 252,000 | - | - |
| Argentina | - | - | 6,161 | 30,805 | - | - | - | - |
| Chile | - | - | - | - | - | - | 800 | 4,000 |
| Mexico | - | - | - | - | - | - | 1,600 | 8,000 |
| Panama | - | - | 675 | 3,375 | - | - | - | - |
| Spain | - | - | - | - | - | - | 40,000 | 200,000 |
| Uruguay | - | - | 2,108 | 10,540 | - | - | - | - |
| | **18,155** | **90,775** | **8,944** | **44,720** | **180,000** | **900,000** | **42,400** | **212,000** |

Subscribed and paid-in capital is held as follows at December 31, 2004:

(In thousands of U.S. dollars)

| Stockholder | Number of Shares | | | Amounts | | | |
|---|---|---|---|---|---|---|---|
| | Series "A" | Series "B" | Series "C" | Series "A" | Series "B" | Series "C" | Total |
| Bolivia | 1 | 20,815 | - | 1,200 | 104,075 | - | 105,275 |
| Colombia | 1 | 74,590 | - | 1,200 | 372,950 | - | 374,150 |
| Ecuador | 1 | 21,553 | - | 1,200 | 107,765 | - | 108,965 |
| Peru | 1 | 76,263 | - | 1,200 | 381,315 | - | 382,515 |
| Venezuela | 1 | 76,264 | - | 1,200 | 381,320 | - | 382,520 |
| Argentina | - | - | 1,630 | - | - | 8,150 | 8,150 |
| Brazil | - | - | 8,496 | - | - | 42,480 | 42,480 |
| Chile | - | - | 278 | - | - | 1,390 | 1,390 |
| Costa Rica | - | - | 2,082 | - | - | 10,410 | 10,410 |
| Jamaica | - | - | 92 | - | - | 460 | 460 |
| Mexico | - | - | 2,983 | - | - | 14,915 | 14,915 |
| Panama | - | - | 1,179 | - | - | 5,895 | 5,895 |
| Paraguay | - | - | 1,156 | - | - | 5,780 | 5,780 |
| Spain | - | - | 9,875 | - | - | 49,375 | 49,375 |
| Trinidad & Tobago | - | - | 133 | - | - | 665 | 665 |
| Uruguay | - | - | 909 | - | - | 4,545 | 4,545 |
| Commercial banks | - | 237 | - | - | 1,185 | - | 1,185 |
| | **5** | **269,722** | **28,813** | **6,000** | **1,348,610** | **144,065** | **1,498,675** |

At December 31, 2004, the distribution of unpaid subscribed capital and of subscribed callable capital is presented below:

(In thousands of U.S. dollars)

| Stockholder | Unpaid Subscribed Capital | | | | Subscribed Callable Capital | | | |
|---|---|---|---|---|---|---|---|---|
| | Series "B" | | Series "C" | | Series "B" | | Series "C" | |
| | Number of shares | Amount | Number of shares | Amount | Number of shares | Amount | Number of shares | Amount |
| Bolivia | 3,169 | 15,845 | - | - | 14,400 | 72,000 | - | - |
| Colombia | 10,222 | 51,110 | - | - | 50,400 | 252,000 | - | - |
| Ecuador | 2,451 | 12,255 | - | - | 14,400 | 72,000 | - | - |
| Peru | 8,620 | 43,100 | - | - | 50,400 | 252,000 | - | - |
| Venezuela | 8,619 | 43,095 | - | - | 50,400 | 252,000 | - | - |
| Argentina | - | - | 794 | 3,970 | - | - | - | - |
| Brazil | - | - | 2,302 | 11,510 | - | - | - | - |
| Chile | - | - | - | - | - | - | 800 | 4,000 |
| Jamaica | - | - | 27 | 135 | - | - | - | - |
| Mexico | - | - | - | - | - | - | 1,600 | 8,000 |
| Spain | - | - | - | - | - | - | 40,000 | 200,000 |
| Uruguay | - | - | 2,745 | 13,725 | - | - | - | - |
| | **33,081** | **165,405** | **5,868** | **29,340** | **180,000** | **900,000** | **42,400** | **212,000** |

### General Reserve

The general reserve was set-up to cover possible contingencies. The stockholders decided to increase the reserve by US$ 145,573 and US$ 99,979 during the years ended December 31, 2005 and 2004, by appropriations from net income for the years ended December 31, 2004 and 2003, respectively.

### Reserve Pursuant to Article No. 42 of the By-laws

The Corporation's by-laws establish that at least 10% of annual net income is to be allocated to a reserve fund until that fund amounts to 50% of the subscribed capital. Additional allocations may be approved by the stockholders. At the stockholders meetings in March 2005 and 2004, it was authorized to increase the reserve by US$ 20,800 and US$ 13,554, from net income for the years ended December 31, 2004 and 2003, respectively.

## (15) Allocations to Stockholders' Funds

The Corporation's board allocate a portion of retained earnings to special funds, created to promote technical cooperation, sustainable human development in the region and management of poverty relief funds.

In March 2005 and 2004, the stockholders agreed to allocate US$ 41,380 and US$ 22,000, from retained earnings at December 31, 2004 and 2003, respectively, to the stockholders' funds.

## (16) Tax Exemptions

The Corporation is exempt from all taxes on income, properties and other assets. It is also exempt from liability related to the payment, withholding or collection of any tax or other levy.

## (17) Derivative Instruments and Hedging Activities

The Corporation seeks to match the maturities of its liabilities to the maturities of its loan portfolio. The Corporation utilizes derivative financial instruments to reduce exposure to interest rate risk and foreign currency risk. The Corporation does not hold or issue derivative financial instruments for trading or speculative purposes.

By using derivative financial instruments to hedge exposures to changes in interest rate and foreign exchange rates, the Corporation exposes itself to credit risk and market risk. Credit risk is the failure of the counterparty to perform under the terms of the derivative contract. When the fair value of a derivative contract is positive, the counterparty owes the Corporation, which creates credit risk for the Corporation. When the fair value of a derivative contract is negative, the Corporation owes the counterparty and, therefore, it does not possess credit risk. The Corporation minimizes the credit risk in derivative instruments by entering into transactions with high-quality counterparties whose credit rating is "A" or higher.

The market risk associated with interest rate and currency risk is managed by swapping loans and borrowings subject to fixed interest rates and denominated in foreign currency into floating interest rate instruments denominated in U.S. dollars. The Corporation enters into derivative instruments with market risk characteristics that are expected to change in a manner that will offset the economic change in value of specifically identified loans, bonds or borrowings and other obligations. Derivative contracts held by the Corporation consist of interest rate and cross-currency swaps and are designated as fair value hedges of specifically identified loans, bonds or borrowings and other obligations with fixed interest rates or non U.S. currency exposure.

The following table presents the notional amount and fair values of interest rate swaps and cross-currency swaps and the underlying hedged items at December 31, 2005 and 2004:

(In thousands of U.S. dollars)

| | Notional amount | | Fair value | |
|---|---|---|---|---|
| | Interest rate swap | Cross-currency swap | Derivative assets | Derivative liabilities |
| **At December 31, 2005 -** | | | | |
| Loans | 30,000 | - | - | 294 |
| Bonds | 1,950,725 | - | 6,071 | - |
| Bonds | - | 1,396,059 | 207,359 | 237 |
| Borrowings and other obligations | - | 19,611 | 1,462 | - |
| Commercial paper | - | 173,844 | 428 | 2,250 |
| | **1,980,725** | **1,589,514** | **215,320** | **2,781** |
| | | | | |
| **At December 31, 2004 -** | | | | |
| Loans | 45,000 | - | 1,677 | - |
| Bonds | 2,048,890 | - | 71,318 | - |
| Bonds | - | 1,384,987 | 516,021 | - |
| Borrowings and other obligations | - | 27,455 | 6,788 | - |
| Commercial paper | - | 119,921 | 3,919 | - |
| Advances and short-term borrowings | - | 262,961 | 26,358 | - |
| | **2,093,890** | **1,795,324** | **626,081** | **-** |

For the years ended December 31, 2005 and 2004 all of the Corporations' derivatives which have been designated in hedging relationships were considered fair value hedges. The change in fair value of such derivative instruments and the change in fair value of hedged items attributable to risk being hedged is included in the statements of income.

## (18) Fair Value

The following table presents the carrying amounts and estimated fair values of the Corporations' financial instruments at December 31, 2005 and 2004. The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties:

(In thousands of U.S. dollars)

| | December 31, 2005 | | 2004 | |
|---|---|---|---|---|
| | Carrying amount | Estimated fair value | Carrying amount | Estimated fair value |
| **Financial assets:** | | | | |
| Cash and due from banks | 1,740 | 1,740 | 2,753 | 2,753 |
| Deposits with banks | 334,571 | 334,571 | 369,990 | 369,990 |
| Trading securities | 1,105,568 | 1,105,568 | 1,017,716 | 1,017,716 |
| Held-to-maturity securities | 87,885 | 87,848 | 166,362 | 166,233 |
| Other investments | 258,576 | 258,576 | 170,521 | 170,521 |
| Loans, net of allowance for losses | 7,185,349 | 7,189,865 | 6,922,322 | 6,937,688 |
| Equity investments | 114,646 | 114,646 | 112,135 | 112,135 |
| Interest and commissions receivable | 181,939 | 181,939 | 151,047 | 151,047 |
| Derivative contracts (included in other assets) | 215,320 | 215,320 | 626,081 | 626,081 |
| **Financial liabilities:** | | | | |
| Deposits | 386,419 | 386,419 | 205,346 | 205,346 |
| Commercial paper | 710,270 | 710,270 | 712,406 | 712,406 |
| Advances and short-term borrowings | 443,707 | 443,707 | 529,190 | 529,190 |
| Bonds | 4,061,108 | 4,065,155 | 4,574,718 | 4,578,908 |
| Borrowings and other obligations | 489,972 | 489,227 | 574,959 | 575,263 |
| Derivative contracts (included in accrued expenses and other liabilities) | 2,781 | 2,781 | - | - |
| Accrued interest and commissions payable | 100,954 | 100,954 | 95,857 | 95,857 |

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

Cash and due from banks, deposits with banks, securities purchased under resale agreements, other assets, deposits, commercial paper, advances and short-term borrowings, accrued interest and commissions, accrued expenses: The carrying amounts approximate fair value because of the short maturity of these instruments.

**Marketable securities:** The fair values of held-to-maturity securities are based on quoted market prices at the reporting date for those or similar securities. Trading securities are carried at fair value based on quoted market prices.

**Loans:** The Corporation is one of the few institutions that offer loans for development in the stockholder countries. A secondary market does not exist for the type of loans granted by the Corporation. As rates on variable rate loans and loan commitments are reset on a semiannual basis, the carrying value, adjusted for credit risk, was determined to be the best estimate of fair value. The fair value of fixed rate loans is determined using the current variable interest rate for similar loans.

**Equity investments:** The fair value of equity investments is determined based on a financial analysis of the investees.

**Derivative assets and liabilities:** Current market prices obtained from third party banks were used to estimate fair values of interest rate and foreign currency swap agreements.

**Bonds, borrowings and other obligations:** The fair value of bonds, borrowings and other obligations is determined using either broker quotes or current rates offered to the Corporation for similar debt of the same remaining maturities.

## (19) Commitments and Contingencies

Commitments and contingencies include the following:

(In thousands of U.S. dollars)

| | December 31, | |
|---|---|---|
| | **2005** | **2004** |
| Credit agreements subscribed | 2,121,192 | 1,569,763 |
| Lines of credit | 811,790 | 507,051 |
| Letters of credit | 11,946 | 20,830 |
| Guarantees | 203,789 | 267,935 |

These commitments and contingencies result from the normal course of the Corporation's business and are related principally to loans and loan equivalents that have been approved or committed for disbursement.

In the ordinary course of business the Corporation has entered into commitments to extend credit. Such financial instruments are recorded as commitments upon signing the corresponding contract and are reported in the financial statements when disbursements are made.

The contracts to extend credit have fixed expiration dates and in some cases expire without making disbursements. Also based on experience, part of the disbursements are made up to two years after the signing of the contract. Therefore, the total commitment amounts do not necessarily represent future cash requirements.

In the event the credit lines are not utilized, no additional cost is incurred by the Corporation.

Guarantees mature as follows:

(In thousands of U.S. dollars)

| | December 31, | |
|---|---|---|
| | **2005** | **2004** |
| Less than one year | 2,850 | 100,000 |
| Between one and two years | 85,333 | 2,850 |
| Between two and three years | - | 83,333 |
| Between three and four years | - | - |
| Between four and five years | - | - |
| Over five years | 115,606 | 81,752 |
| | 203,789 | 267,935 |

Guarantees result from the normal course of the Corporation's business and usually take the form of partial guarantees to CAF's clients, as a credit enhancement for their liabilities, as well as guarantees to third parties on behalf of the Corporation's clients. CAF's responsibility is usually limited to payment up to the amount of the guarantee upon default by the client. The carrying value of the guarantees at December 31, 2005 and 2004 was nil.

Litigation filed by a German banking institution and its US wholly owned subsidiary is currently pending against CAF in the U.S. District Court for the Southern District of New York, whereby plaintiffs allege a breach of contract and a breach of implied covenants of good faith in relation to certain negotiations concerning a potential purchase and sale of promissory notes issued by a Mexican company in bankruptcy proceedings under Mexican law. Plaintiffs requested damages in an amount of not less than US $ 1,000 (one millions dollars). CAF is contesting this claim, relative to both liability and damages, and does not believe the outcome of this case will have a material adverse effect on the Corporation´s financial condition or results of operations.

# Governing Bodies

Corporación Andina de Fomento.

## Shareholders Assembly[1]

The Shareholders Assembly is the highest authority of CAF. Shareholders meetings can be regular -taking place once a year within ninety days following the end of the fiscal year- or Special. In both cases, the meetings are convened by the Executive President. The Assembly is composed of Series "A", "B" and "C" shareholders. Series "A" and Series "B" shares have been subscribed by the governments of the five member countries or by public, semi-public or private institutions. Series "C" shares can be subscribed by governments or public and private institutions of countries outside the Andean region as well as by international organizations. The Assembly approves the annual report of the Board of Directors, and the audited financial statements, and determines the use of CAF's profits. It also elects the Board Members (in accordance with the provisions set forth in the Constitutive Agreement), appoints external auditors, and examines any other issues expressly submitted to it.

## Board of Directors[2]

The Board of Directors consists of thirteen members and their alternates. Ten of its members are elected by shareholders of Series "A" and "B" for a three-year period and can be re-elected. Two Directors and their alternates are elected by the holders of Series "C" shares. The private banking and financial institutions of the sub region which hold Series "B" shares of the Corporation appoint one director and his alternate. The Board of Directors shall have the power to establish the policies of the Corporation and to appoint the Executive President, as well as to approve credit operations, the annual expense budget, the granting of guarantees or investments, and any other operation within CAF's objectives. Approval of certain operations is delegated to the Executive Committee or to the Executive President in accordance to the rules set forth by the Board of Directors.

## Executive Committee

The Executive Committee was created by the Board of Directors in 1971. It consists of six directors appointed by Series "A" and "B" shareholders and is chaired by the Executive President. It is in charge of approving financial operations not exceeding the limits set forth by the Board of Directors.

## Audit Committee

The Audit Committee was established by the Board of Directors in 1996. It consists of six members: the Chairman of the Board, who presides the Committee; four (4) directors elected by the Board and CAF's Executive President. The Committee recommends the selection and hiring of external auditors, and studies their annual work plan; it also reviews CAF's annual report and externally audited Financial Statements before these are submitted for approval to the Board and the Assembly; it reviews External Audit reports dealing with topics relevant to the effectiveness of the structure of internal control systems; and it also reviews the annual program for investment portfolio risk management and control, and the annual report on this program's execution.

## Executive President

The Executive President is CAF's legal representative. He is in charge of the Corporation's general direction and management as well as all matters which have not been specifically entrusted to any other governing body. Likewise, he approves the strategic country and sector plans the institutional structures and processes under his authority, and the Corporation's financial operations within the limits delegated to him by the Board of Directors. The Executive President is assisted by an Advisory Council composed of experts from the economic, business and financial communities of the region, whose main task is to support the President in the analysis of CAF's strategic objectives. The Executive President is appointed for a five-year period and can be re-elected.

**1** The 36th meeting of the Shareholder's Regular Assembly was held on March 8, 2005, and the 10th meeting of the Shareholder's Extraordinary Assembly was held on June 6, 2005.

**2** During 2005, the Board of Directors held four meetings: March 8, August 15, October 24 and December 6.

# Board of Directors
(as of December 31, 2005)

President of the Board of Directors (2005-2006) [1/2]
Waldo Gutiérrez
Minister of Finance, Bolivia

**SERIE "A" Shareholders**

**BOLIVIA**
Principal: Waldo Gutiérrez
Minister of Finance
Alternate: Rodrigo Castro Otto
Vice Minister of Public Investment and External Financing

**COLOMBIA**
Principal: Alberto Carrasquilla
Minister of Finance and Public Credit
Alternate: Jorge Humberto Botero
Minister of Foreign Trade

**ECUADOR**
Principal: Galo Montaño
President of the Board of Directors of Corporación Financiera Nacional
Alternate: Enrique Fócil
Vice Minister of the Ministry of Foreign Trade, Industrialization and Fisheries

**PERU**
Principal: Alfredo Ferrero Diez Canseco
Minister of Foreign Trade and Tourism
Alternate: Fernando Zavala Lombardi
Minister of the Economy and Finance

**VENEZUELA**
Principal: Nelson Merentes
Minister of Finance
Alternate: Jorge Giordani
Minister of Planning and Development

**SERIE "B" Shareholders**

**BOLIVIA**
Principal: Carlos Díaz Villavicencio
Minister of Economic Development
Alternate: Juan Antonio Morales
President of Banco Central de Bolivia

**1** Through March, 2005, the Board was chaired by Nelson Merentes. Minister of Finance, Venezuela.
**2** Through July, 2005, the Board was chaired by Luis Carlos Jemio, Minister of Finance, Bolivia.

**COLOMBIA**

Principal: José Darío Uribe
General Manager of Banco de la República

Alternate: Santiago Montenegro
National Director of the Planning Department

**ECUADOR**

Principal: Magdalena Berreiro
Minister of the Economy and Finance

Alternate: Mauricio Pareja
Acting General Manager of Banco Central del Ecuador

**PERU**

Principal: Daniel Schydlowsky R.
President of the Board of Directors of Corporación Financiera de Desarrollo (COFIDE)

Alternate: Waldo Mendoza
Vice Minister of Finance. Ministry of Economics and Finance

**VENEZUELA**

Principal: Edmeé Betancourt de García
Minister of Light Industries and Commerce

Alternate: Edgar Hernández Behrens
President of Banco de Desarrollo Económico y Social de Venezuela

**SERIE "C" Shareholders**

**BRASIL**

Principal: José Carlos Rocha Miranda
Secretary of International Affairs. Ministry of Planning, Budget and Process

**COSTA RICA**

Alternate: Francisco de Paula Gutiérrez
President of Banco Central de Costa Rica

**MEXICO**

Alternate: Miguel Hakim Simón
Under Secretary for Latin America and the Caribbean. Secretary for International Affairs

**SPAIN**

Principal: Pedro Solbes Mira
Second Vice President of the Government and Minister of the Economy and Finance

**PRIVATE BANK**

Principal: Guillermo Lasso
Executive President of Banco de Guayaquil Ecuador

Alternate: José Antonio Colomer
Managing Director of BBVA Banco Continental Peru

# Management
(as of December 31, 2005)

**President and Chief Executive Officer** L. Enrique García
**Executive Vice President** Luis Enrique Berrizbeitia
**General Advisor** Luis Sánchez Masi
**Chief Legal Counsel** Fernando Dongilio

**Corporate Comptroller** Marcelo Zalles
**Director, Risk Management** Camilo Arenas
**Director, Internal Audit** Paola Gennari

**Chief Credit Officer** Stephen Foley
**Director, Special Assets** Renny López

**Director, Secretariat and Corporate Communications** José Luis Ramírez
**Director, Cultural and Community Development** Ana Mercedes Botero

**Corporate Vice President, Development Strategies and Chief Economist**
**Director, Economic Studies** Luis Miguel Castilla

**Corporate Vice President, Country Programs** Lilliana Canale
**Director, Regional Programs** Alexis Gómez
**Director, Governance and Technical Cooperation** Elvira Lupo
**Country Representative, Bolivia** José Carrera
**Country Representative, Brazil** José Vicente Maldonado
**Country Representative, Colombia** Freddy Rojas
**Country Representative, Ecuador** Luis Palau
**Country Representative, Peru** Germán Jaramillo
**Assistant Representative, Peru** Ricardo Campins

**Corporate Vice President, Infrastructure** Antonio Juan Sosa
**Director, Projects** Manuel Llosa
**Director, Sectoral Analysis and Programming** Rolando Terrazas

**Corporate Vice President, Corporate Finance and Investment Banking** Peter Vonk
**Director, Structured Financing** Carmen Elena Carbonell
**Director, Financial Institutions and Capital Markets** Félix Bergel
**Director, Corporate Banking** Jesús Miramón

**Corporate Vice President, Social and Environmental Development** Claudia Martínez
**Director, Social Development** Bernardo Requena
**Director, Environment** María Teresa Szauer
**Director, SMEs and Microfinance** Manuel Malaret

**Corporate Vice President, Chief Financial Officer** Hugo Sarmiento
**Director, Financial Policies and International Issues** Gabriel Felpeto
**Director, Multilateral and Bank Financing** Fernando Infante
**Director, Treasury** Eleonora Silva
**Director, Accounting and Budget** Marcos Subía

**Director, Operations Control** Germán Alzate
**Director, Human Resources** Seyril Siegel
**Director, Information Technology** Esteban Cover
**Director, General Services** Jaime Caycedo

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