

ANNUAL REPORT 2016



nacional financiera
Banca de Desarrollo



Board of Directors and Commissioners as of December 31, 2016

BOARD MEMBERS SERIES "A"	
HOLDERS	DEPUTIES
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VANESSA RUBIO MÁRQUEZ Deputy Minister of SHCP	ALBERTO TORRES GARCÍA Head of the Public Credit Unit, SHCP
ILDEFONSO GUAJARDO VILLARREAL Minister of Economics	ENRIQUE EDGARDO JACOB ROCHA Chairman of the Entrepreneur National Institution Ministry of Economics
PEDRO JOAQUÍN COLDWELL Minister of Energy	CÉSAR EMILIANO HERNÁNDEZ OCHOA Deputy Secretary of Electricity Ministry of Energy
JESÚS ALAN ELIZONDO FLORES General Director for the Financial System Banco de México	RAÚL JOEL OROZCO LÓPEZ Director of Promotion - Financial Intermediaries Banco de México
ENRIQUE CABRERO MENDOZA General Director National Council for Science and Technology (CONACYT)	OSCAR ERNESTO VELA TREVIÑO Head of Insurance, Pension and Social Security, SHCP

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MANUEL JESÚS HERRERA VEGA Chairman of Mexican Industrial Chambers Confederation (CONCAMIN)	ENRIQUE GUILLÉN MONDRAGÓN Chairman of the National Chamber of the Transformation Industry (CANACINTRA)
ENRIQUE SOLANA SENTÍES Chairman of the Confederation of National Chambers of Commerce, Service and Tourism (CONCANACO-SERVYTUR)	GUSTAVO ADOLFO DE HOYOS WALTHER Chairman of the Mexican Employers Confederation (COPARMEX)



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THERE ARE ONLY INDEPENDENT DEPUTIES

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CFO of América Móvil, S.A.B. de C.V.

JOSÉ SALVADOR MARTÍNEZ CERVANTES
Independent Professional

STATUTORY AUDITORS

HOLDERS

DEPUTIES

SERIES "A"

RODRIGO ALFONSO SÁNCHEZ MÚJICA
Regular Public Statutory Auditor
Ministry of Public Affairs

FIDEL RAMÍREZ ROSALES
Deputy Public Statutory
Ministry of Public Affairs

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IGNACIO NÚÑEZ ANTA
Comptroller and Manager of Grupo Financiero Anáhuac

SECRETARY OF THE BOARD OF DIRECTORS

LÁZARO JIMÉNEZ GARCÍA
Secretary of the Board of Directors

PERLA LILIANA DE LA PEÑA AMANTE
Deputy Secretary of the Board of Directors



Officers attending the Board of Directors Meetings as of December 31, 2016

JACQUES ROGOZINSKI SHTULMAN

General Director (CEO)

CATALINA BONNEFOI MONROY

Deputy General Director of Development Finance

RAÚL SOLÍS WOLFOWITZ

Deputy General Director of Investment Banking

PEDRO GUERRA MENÉNDEZ

Deputy General Director of Treasury and Financial Markets

PEDRO A. ARGÜELLES RODRÍGUEZ MONCADA

Deputy General Director of Credit

JOSÉ ELÍAS SAHAB JAIK

Deputy General Director of Regional Promotion and Institutional Relations

TONATIUH SALINAS MUÑOZ

Deputy General Director of Entrepreneurial Banking

LUIS DANTÓN MARTÍNEZ CORRES

Deputy General Director of Legal and Fiduciary Affairs

FEDERICO BALLÍ GONZÁLEZ

Deputy General Director of Finance and Management

ADRIANA COVARRUBIAS DEL PERAL

Technical Coordinator of the CEO

LÁZARO JIMÉNEZ GARCÍA

Secretary of the Board of Directors

PERLA LILIANA DE LA PEÑA AMANTE

Deputy Secretary of the Board of Directors



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MESSAGE FROM THE GENERAL DIRECTOR

NACIONAL FINANCIERA

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Uncertainty and volatility of finance markets were a constant during 2016. Nevertheless, in spite of this hostile context, Nacional Financiera stood on track and continued achieving the objectives established by the mandate of President Enrique Peña Nieto. Our plan has been successful: we have reached more financing at the lowest possible cost for the enterprises in Mexico.

Nafin surpassed the target credit and guarantee balance expected for this year. As of December 31, 2016 we registered 373,475 billion pesos, that is, in nominal terms, 71.5% in respect of December 2012 and 15.6% more than the one registered on 2015.

Such increase allowed us to serve 715,741 beneficiaries, 34% more than those of 2015. These beneficiaries included 170,816 enterprises and 544,925 microcredits; 99.8% of these enterprises were micro, small and medium-sized. Such results were possible thanks to the implementation of our innovative strategies.

In 2016, Nacional Financiera listed the first green bond in the Mexican Stock Exchange, in pesos. This bond will allow to continue financing the development of sustainable

projects such as eolian and solar parks. This bond was issued for 2,000 billion pesos, in a period of 7 years at an interest rate of 6.05%.

This operation is additional to our first green bond issued in 2015, listed in the international markets. A year later, this transaction granted Nacional Financiera the “Green Bond of the Year” award by “Environmental Finance”, as well as a distinction by Euromoney for the best transaction of the year of such kind.

Together with this innovative spirit, new schemes were implemented in order to promote financial inclusion for women and young people by increasing the age range from 30 to 35 years old in the “Credit for Young People” program.

Furthermore, to promote innovation within Mexican young people, we launched the competition “*Reto Aplicando México*”. This was performed to stimulate and recognize the local talent to develop digital applications on finance subjects.

These additional actions and programs directed to youth included and launched “*Fondo Ángel*” of seed capital



together with the Government of Mexico City, whose objective is to promote the development of innovative and high impact projects among young people.

In 2016, Nacional Financiera ratified its key roll to develop the entrepreneurial structure of Mexico. Thus, it expanded the services for women, such as the “*Mujer Pyme*” program. This program seeks to develop and consolidate micro, small and medium-sized enterprises lead by women. Therefore, in 2016, 3,000 credits for an amount greater than 2,500 billion pesos were placed.

Our services did not stop increasing in order to satisfy the needs of Nafin clients. Public and private enterprises increased its use of our e-factoring platform, Productive Chains, to 14.3% in 2016 in respect to 2015.

National companies such as the Airport Group of Mexico City, and international companies such as the British company Greensill Capital are now our clients.

We complement our financing activity with promotion, training and technical assistance schemes. Three Nafin mobile office units went across the country to provide 1,166 courses to train more than 19,000 beneficiaries.

As a complement of this extension strategy, we implemented a new Entrepreneurial Development Centre to permanently serve entrepreneurs, start-ups and financial intermediaries.

In relation to our Training and Technical Assistance program, during 2016, two Corporate Government workshops for family companies were given and a largescale conference attended by more than 360 businesspeople and Nacional Financiera consultant advisors was held.

As part of the international agenda, a memorandum of understanding was signed between Nacional Financiera and the KfW Development Bank (Germany) for sharing knowledge and exchanging best practices in green financing.

We also developed the Second International Program on Best Practices for Development Banking with the participation of 24 worldwide development banks and financial institutions.

It is worth mentioning that the results reached in 2016 were obtained without jeopardizing the institution’s financial stability. The overdue portfolio index at the end of 2016 was only 1.09% and the capitalization level reached 13.2%.

There was a net profit of 1,321 billion pesos in addition to the 800 million pesos delivered to Mexico’s Ministry of Finance and Public Credit as resource leveraging pursuant to the authority conferred by the legislation in force which resulted in a return on equity of 7.1% in 2016.

Finally, I would like to thank the Nacional Financiera personnel for their work and commitment since they are the most important asset of this institution, and also to the Ministry of Finance and Public Credit authorities for supporting the achievement of the results herein.

Even though 2017 means another year of uncertainty, we will continue to move forward. We will continue working towards the compliance of the authorized goals and keeping up with the growth rate, as established in the medium-term institutional program together with the major objectives set forth in the National Development Plan and within the framework of Mexico’s Financial Reform for Mexican companies to continue having access to greater credits.

We will enhance our presence within the international markets by issuing new funding instruments for the credit portfolio and we will continue supporting the financial breakthrough expected by the government before the end of the current administration.

This is not an easy challenge; nevertheless, our 80 years’ experience will allow the institution to continue contributing to the development of the country.

Jacques Rogozinski S.

CEO



ECONOMIC ENVIRONMENT

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At the end of 2016, the growth of the world economy was 3.1%, less than that recorded in 2015, i.e. 3.2%, and below year start expectations of 3.4%.

Every year, three factors have defined post-crisis recovery: below expectations growth, lower growth rates and a disparity in the growth of different countries, regions and types of countries.

Developed economies grew 1.6% (2.6% in 2015), United States 1.6% (2.6% in 2015), the Euro Zone 1.7% (2% in 2015), Japan 0.9% (1.2% in 2015), United Kingdom 2.0% (2.2% in 2015) and Canada 1.3% (0.9% in 2015).

Emerging economies as a whole had a 4.1% growth, equal to previous year. Disparity between countries, however, is huge. For example, BRICS; Brazil is in recession with -3.5%, after -3.8% in 2015; Russia had a contraction of -0.5%, after decreasing -3% in 2015; India grew 6.6%, when 7.6% was reached in 2015; China grew 6.7% (6.9% in 2015) and South Africa only 0.3% (1.3% in 2015).

The US economy continued to be driven by private consumption, which in 2016 grew at an average annual rate

of 2.7%. Factors underpinning household spending were strengthened: non-farm payrolls grew by 2.16 million jobs and the hourly wage rose at a real rate annual average of 0.8%, consumer credit increased by 234.2 billion dollars, housing prices rose about 5% and the S&P 500 grew 9.5%.

It is worth stopping in the labor market behavior. Since October 2010, non-farm payroll has grown continuously, accumulating 14 million 931 new jobs, closing the year with 145 million 147 thousand jobs, which meant the maximum historic level of non-agricultural employment in the United States. Thus, the unemployment rate ended 2016 at 4.7% of the Economically Active Population, down by three tenths of a percentage point in relation to that recorded in 2015. It is noteworthy that these figures would indicate the economy has rapidly approached its full employment level.

Moreover, inflation in the first half of the year was limited by the fall in fuel prices, but showing a rebound in the second half. As measured by Consumer Price Index (CPI), annual inflation closed at 2.07% in 2016, which was its highest level since 2011, while core inflation, which does not consider food and fuel, ended at 2.2%, its highest since 2011.



In the Euro zone, measures taken by the European Central Bank (ECB) seem to have begun improving. The region as a whole would have recorded its third consecutive year of growth, advancing 1.7%. According to estimates, all countries in the region have grown in 2016, at very different rhythms, though, from Luxembourg with a rate of 3.5%, Spain 3.2%, Germany 1.7% to Italy with 0.9% and Greece with 0.2%.

Annual inflation in the region was 1.1% at the end of 2016, the highest since 2012. While it is still far from the target of 2.0%, this 2016 upward trend to some extent reduced the risk of deflation and has generated more favorable expectations about the effectiveness of decisions taken by ECB.

The UK economy, despite the impasse from the referendum to remain in the European Union, again finished as the best in the G-7, growing at a rate of 2%. Private consumption rose at an annual rate of 2.8%, the highest for a calendar year since 2007. Apparently, negative expectations generated with Brexit had no immediate effect on economic activity.

Japan resumed growth, but lower than previous year's rate. Fiscal and monetary stimuli have failed to lift the economy from a long slumber, so the risk of deflation remains latent. At the end of 2016, the annual consumer inflation was 0.3%.

As for emerging economies, it can be noted that China's economy continued to show a strong divergence inside, with the primary and tertiary sectors showing signs of weakness, while the secondary sector showed acceleration. Also, the Chinese government continued to implement fiscal and credit stimulus measures. As for Brazil, throughout the year, weak domestic demand was persistent, result largely from the deteriorating labor market, continued credit restrictions and the slow recovery in confidence levels, which fell sharply by scandals of corruption that forced their president's departure. Regarding Russia, the turnaround in oil prices gave a boost to economic activity, which however was not enough to prevent another year of contraction. The weakness of the ruble accumulated in the previous two years and conflicts of international politics caused a supply constraint, affecting the domestic market and also causing high inflation. Finally, the economies of Latin America had a

distinct growth. In addition to the already mentioned Brazil, Venezuela, Ecuador and Argentina presented contraction, while Chile, Colombia, Bolivia and Peru moved at rates between 1.5% and 3.9%. In terms of inflation, Venezuela's went up 345%, followed by Argentina with 40% and Uruguay 10%, while inflation of Ecuador, Peru and Chile was placed between 2-4%. Colombia and Brazil had rates between 7-9%.

The continued divergence between phases of the economic cycle, growth rates and inflation also meant a dynamic discrepancy on monetary policy measures taken. While the Federal Reserve System (Fed,) although until the last month of the year, continued its monetary policy normalization by increasing again 25 base points (bp) on the target range for its reference rate (0.50% - 0.75%). Bank of Japan and ECB tightened its monetary stimulus measures. The Bank of England cut its rate to soften the effects of Brexit. The central banks of Latin America maintained a restrictive bias against inflationary spikes and Asia's favored some relaxation, due to low inflationary pressure and a downturn in growth expectations.

Mexican Economy

At the end of the year, Mexico's economy grew 2.3%, lower than the rate recorded in 2015, 2.5% and below expectations at the start of the year, which were located at 2.7%.

Private consumption was again the engine of growth in Mexico, advancing until the third quarter at an average annual rate of 2.9%. The improvement in real wages, as a result of low inflation in 2015 and almost all of 2016; an increase in consumer credit, which grew at a rate of 8.7%, as well as international remittances, which in 2016 set a new record high to reach 26.97 billion US dollars, equivalent to nearly 504 billion pesos.

Fixed investment remained sluggish. At November 2016 showed an average growth of only 0.4%, with construction investment falling -0.1% and that for machinery and equipment growing by 1.1%.

The external sector had not one of its best years. Exports contracted by -1.8%, despite the strong adjustment suffered by the exchange rate. Undoubtedly the external



environment was unfavorable. The fall in oil prices, the slowdown in manufacturing activity in the United States, uncertainty about the Brexit and presidential elections of our northern neighbor, all affected the expectations of the companies involved in this sector.

On 24 June, to strengthen the macroeconomic position of the country in response to the potential consequences of UK departure from the European Union, the Mexican Ministry of Finance (SHCP) announced a second preventive adjustment programmable spending exclusively on the Federal Government, by 31.715 billion pesos. Prior to this, SHCP cut spending for 2016 on 132 billion pesos, 100 billion of them in investment spending at Petroleos Mexicanos (Pemex,) given the high volatility that presented the international financial markets in the first months of the year, thereby giving the signal of strengthening macroeconomic fundamentals, doing so in coordination with the Bank of Mexico, which took the corresponding monetary policy measures.

The overall annual rate of inflation accelerated in the last four months of the year, largely as a result of increases in administered prices of goods and services, as well as an increase transfer from exchange rate to final consumer prices. At the end of the year, annual inflation was 3.36%,

which represented an increase of 1.23% over that recorded in 2015, while core inflation was 3.44%, the highest for a full year since 2010.

As for monetary policy, the Bank of Mexico raised its benchmark rate in February to help strengthen macroeconomic fundamentals and avoid imbalances that result in instability and deterioration of expectations, particularly inflation, especially when the exchange rate exceeded the 19 pesos barrier per dollar.

Finally, as far as terms of monetary policy is concerned, the Bank of Mexico raised its benchmark rate by 250 bp during the year, 100 in the first half and 150 in the second. Strengthening macroeconomic stability was one of the most important premises of the monetary authorities' strategy, since the speed of the upward trend in the exchange rate seemed inconsistent with the fundamentals of the Mexican economy, especially the quotes reaction to specific events such as the sharp drop in oil prices, the Brexit and even Donald Trump's triumph as US President. In addition, increases in the second half also sought to halt a deterioration of inflation expectations, and that applied in December, specifically trying to maintain proper differential against the reference rate of the Federal Reserve after raising its rate by 25 bp.

PYMMES

PROMOTION

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Promotion Program

Nafin, through its different credit and guarantees programs, channeled resources in 2016 of 556.489 billion Mexican pesos, of which 51.5% corresponded to Second-Tier loans, 44.1% to Guarantees and 4.4% to First-Tier and Public Sector loans.

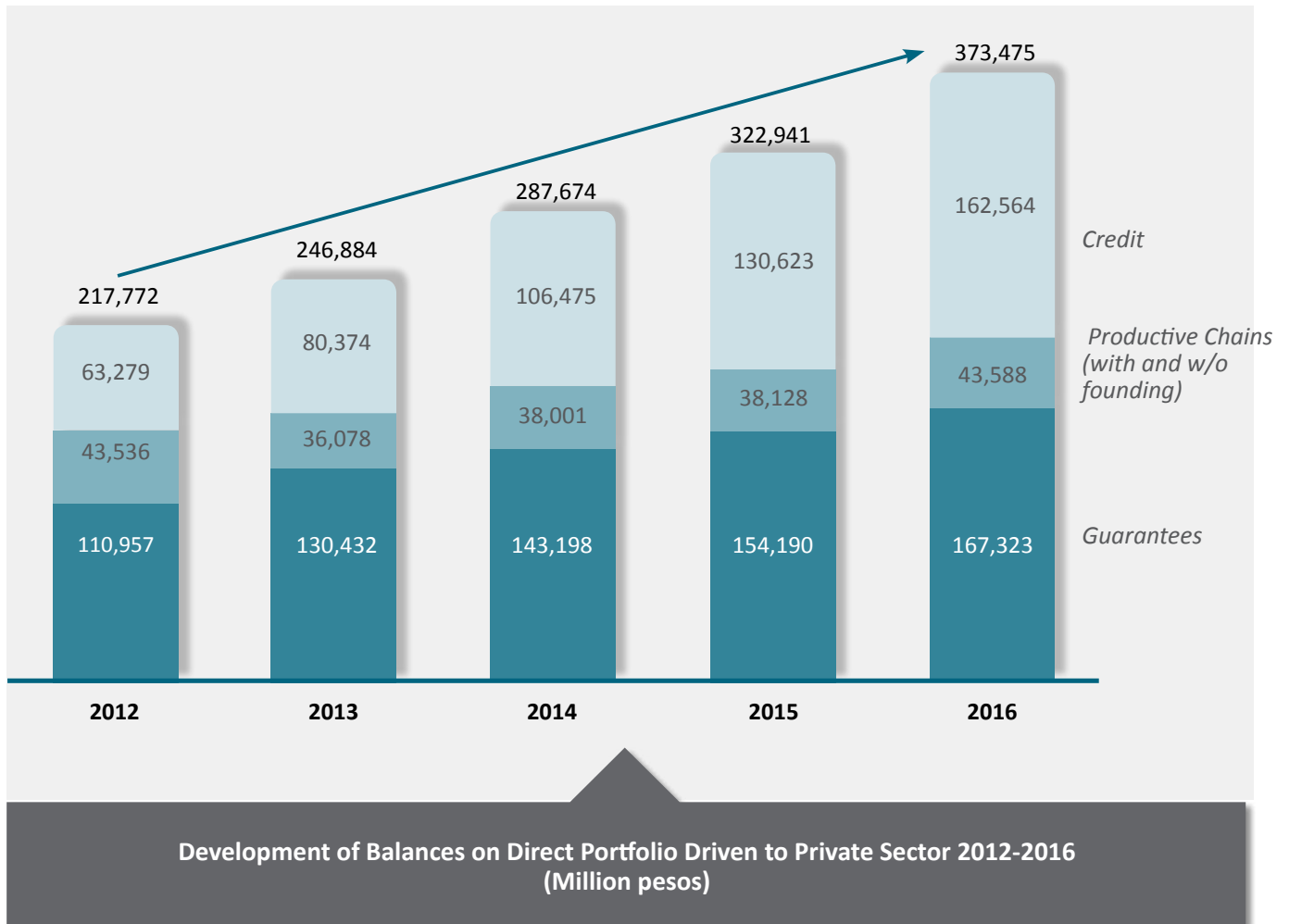
Credit and Guarantees to Private Sector Program

With the variety of products offered by Nafin through its Productive Chains, Traditional Discount, Micro-Business Financing and Equipment programs, as well as its Guarantees Scheme and the credit guaranteed by the later, a total of 550.789 billion pesos were channeled to the private sector, reaching 715,741 beneficiaries, including 170,816 businesses

and 544,925 micro-loans. Of the total beneficiaries, 99.8% were micro, small and medium-sized enterprises (SMEs).

Through the Second-tier loans, Productive Chains participated with a credit granting of 191,640 billion pesos, Micro-Businesses and Equipment with 30,935 billion pesos and the Traditional Discount (Factoring) with 64,025 billion pesos.

This program stimulates the granting of loans to SMEs, as Nafin participates on the risk over financings granted by the Financial Intermediaries (FI). During the period from January to December 2016, a total of 245,415 billion pesos was channeled (including guarantees financing and guaranteed credit). Thus, the balance at the end of the period, considering guaranteed credit, was 167,323 billion pesos, 8.5% above the balance at the end of December 2015. Of this balance, there is coverage of the Nafin Guarantee of 38%.



Productive Chains Program

At the end of December 2016, 191,640 billion pesos were granted to the Productive Chain Program, which generated a balance of 43,588 billion pesos at year end. Under the Program, the agencies of the Federal Government in 2016 recorded accounts payable amounting 353,373 billion; of which 27% was collected in advance. This allowed to support 5,133 suppliers who exercised the benefit of the advance payment through financial factoring.

During 2016, the main indicators of the program are as follows:

- 14.3% increase in the total balance, in relation with 2015.
- More than 500 First Order Companies (EPO) in operation, benefiting 23,000 suppliers.
- More than 2.4 million documents were operated.

Promotion activity continued to grow, recording in 2016 a total of 42 new chains and 186 in the promotion and implementation phase.



The main results are as follows, compared to the same period last year:

- The Industrial and Construction Sector registered a 2,264 billion pesos operation increase, equivalent to 12%.
- The Federal Government recorded an annual increase in operation of 5,720 billion, or 6%.
- Incorporating Greensill Capital, first foreign FI platform for productive chains. In 6 months operated 1 billion pesos with 18 suppliers.

Signing of a Collaboration Agreement with Mexico City's Airport Group (CMAG). Seven CMAG providers already operate factoring, two in implementation and 25 in promoting.

Sector-based Programs

Nafin offers programs to support Micro, Small and Medium Enterprises (MSMEs) in economic sectors or activities with limited access to financing, as well as foster job creation and contribute to providing services to strategic and high-priority sectors. At the close of 2016, these programs reached a record balance of 19,375 billion pesos, a growth of 20% compared to 2015, caused by the granting of 29,963 credits amounting 13,904 billion pesos. By line of action, the main results are as follows:

i. Modernization and Equipment. 14,682 credits have been granted for 4,089 billion pesos. Highlighting the following program:

- **Car Industry:** In supporting the acquisition of utility and light commercial vehicles, 14,087 credits were granted amounting 3,127 billion pesos. For the acquisition of units for federal motor carrier cargo, passengers and tourism, 327 credits were granted for 717 million pesos.

ii. Financial Inclusion. 5,957 credits have been granted for 3,537 billion pesos, highlighting the following programs:

- **Support Program for Women Entrepreneurs:** Incorporating a gender perspective in the supply of credit to MSMEs, to promote competitiveness and growth of women who run business in the country. 3,501 credits with a total of 2.721 billion pesos granted.

- **Credit for Young People:** Provides credit to young people between 18 and 35 years old who want to start or grow a business they already have. 1,983 credits with a total of 631 million pesos granted.

iii. Supplier Development. 1,659 credits have been granted for 3,026 billion pesos, highlighting the following programs:

- **Support Program for Construction Sector:** It supports building companies dedicated to the development of commercial infrastructure. 1,289 credits with a total of 2,311 billions pesos granted.
- **Support Program to Leather, Footwear and its Productive chain:** It supports the production chain of leather and footwear sector funding to promote technological development, operational and administrative modernization. 207 credits with a total of 277 million pesos granted.

iv. Regional Development. 2,236 credits have been granted for 2,882 billion pesos, highlighting the following programs:

- **Economic Boost Program and Employment Promotion:** It is run in coordination with participating state governments, and is aimed at assisting their high-priority economic activities and contributing to regional development and job creation: 1,597 credits with a total of 2,056 million pesos granted.

State	Loans Granted	Placed Amount (million pesos)
Oaxaca*	458	489
Michoacán*	325	426
Chiapas*	308	493
Aguascalientes	212	218
Guerrero*	89	153
Sinaloa	73	97
Zacatecas	66	75
Estado de México	31	52
Yucatán	25	42
Nuevo León	5	5
Tamaulipas	5	5
Total	1,597	2,056

* In these states the program is aligned to the federal strategy of "Special Economic Zones."



Notably, during 2016 the states of Queretaro, Nuevo Leon, Guanajuato, Jalisco, San Luis Potosi and Hidalgo were incorporated into this scheme.

- **Program for Financing Economic Boost in Border Areas:** Implemented to facilitate financing in competitive conditions to businesses in the states located along Mexico's northern and southern borders: Baja California, Baja California Sur, Sonora, Chihuahua, Tamaulipas, Coahuila, Chiapas, Quintana Roo, Campeche and Tabasco. 473 credits with a total of 620 million pesos granted. It should be noted that operations in Chiapas, Campeche and Tabasco ended in July 2016.

v. Sustainable Financing. Through the Program Eco-Business Credit for Energy Efficiency in its "massive" and "individualized" modes, support micro and small companies are supported for the acquisition and/or replacement of efficient equipment, aimed at generating savings in electricity. 5,328 credits with a total of 262 million pesos granted.

vi. Economic Reactivation. 101 credits have been granted for 108 million pesos, highlighting the following programs:

- **Financing Program for Economic Reactivation of Campeche and Tabasco:** It was implemented as part of a series of measures by both the Federal and state governments to counter the impact of falling oil prices on their economies. 62 credits with a total of 63 million pesos granted.
- **Financing Program for Economic Reactivation of Companies Affected by Natural Disasters:** It supported MSMEs affected by Hurricane "Marty" in Sonora. 39 credits with a total of 45 million pesos granted.

Sector-based Programs Promotion

It develops and implements strategies for promotion and sales of certain sector-base programs through a Promoters Network, highlighting Economic Boost and Emerging programs and those designed to strengthen some economic sector, such as Credit for Young People, Business Women, Leather and Footwear, Financing to Higher

Education, Come to Eat, and the Stimulus to Good Taxpayers. In the period from January to December 2016, more than 9,000 companies were supported with a spending of 9,352 billion pesos by the above programs.

Promotion of Factoring

It creates and implements strategies for promotion and affiliation to Factoring Programs in Productive Chains and Financing Suppliers using the Promoters Network and Customer Service Center via telemarketing campaigns, mails, events and modules installed in EPO Companies.

The main results are as follows:

- Affiliation of 4,646 new suppliers in Productive Chain Programs.
- 92% of suppliers recorded operations.

Administration of Electronic Products

It controls Management platforms and Document management, as well as Nafinet, a platform on which products of Productive Chains, Financing to Distributors and Electronic Credit are electronically operated, as well as training, expert advice and support is provided to financial intermediaries, EPO companies and internal areas. It also makes the review of membership records to Productive Chains and certain sectoral programs.

Some of the volumes of platforms include:

- Supervision and monitoring of more than 9,500 average daily operations (Chains and Credit at Fixed Rate, Variable Rate, Emerging and Microcredit) with amounts of more than 900 million pesos a day.
- Care and support to more than 60 bank and non-bank financial intermediaries for credit transactions and queries.
- Dispersion of funds to SMEs and FIs with an average of more than 740 million pesos monthly on behalf of EPOs through Productive Chains.
- Implementation of more than 19 Productive Chains.



Customer Services and Channels Development

It hires and manages the Center for Customer Service and Trust 80444 “Technical Assistance Fund for Financing Programs” through which the areas of Sector Promotion and Factoring have resources for the implementation of strategies for promotion and care of different programs.

The main results in 2016 are as follows:

- 234,794 calls were received, of which 77% are users of Productive Chain Program.
- Productive Chain providers conducted discount of invoices by phone amounting 29.094 billion pesos, which represents 13% of the total operated in the Program.
- Through the Entrepreneur Support Network, 10,307 applications were handled, of which 88% required training services and 12% financing. Of the 1,237 corresponding to financing, 94% did not meet the requirements and 6% of applications were channeled to commercial banks.

Venture Capital

It promotes investment in innovation projects and high impact on the economy directly and through investment funds. It is composed of six portfolios: Conacyt-Nafin Fund, the Seed Capital Joint Venture, Venture Capital Ecosystem Inadem-Nafin, Crowdfunding Project, Mexico-Ventures Fund and IMPI-Fumec Support Program for Patenting. They are managed and operated by participating in boards of directors and shareholders’ meetings of companies, investment committees of funds and follow-up meetings with funding entities. They have supported 180 companies that generate 6,479 jobs.

The main results are:

- **Conacyt-Nafin Fund.** The program’s total investment was 224 million pesos in 43 companies. It is currently in phase of disinvestment. It has negotiated the disinvestment in eight companies for a total of 54 million pesos, two of which were in 2016, for a total amount of 8 million pesos.
- **Seed Capital Joint Venture Fund.** 290 million pesos for seven investment funds, which have supported 49

companies. 16 were supported directly with 79 million pesos with two successful exits.

In 2016, the most significant transactions were:

- ✓ Formalizing three investment funds amounting to 124 million pesos.
- ✓ Investment in Actividades Mexico Fund, and through other funds, six companies were supported.
- ✓ Negotiation the exit of Natgas for 11.3 million pesos.
- ✓ Formalizing contributions to Mexico City Fund and Government of Jalisco Fund with contributions of 48 and 90 million pesos, respectively.
- ✓ Venture Capital Ecosystem Inadem-Nafin. The total amount of the Program is 5,081 billion pesos (public and private resources) with a participation of the Entrepreneur Capital Trust Fund of 1,758 billion pesos to support 41 investment funds. Funds have invested in 103 companies. During 2016, seven funds totaling 813 million pesos were formalized, of which 249 million pesos come from public resources.

Crowdfunding Project. Diagnosing Crowdfunding platforms in Mexico in conjunction with Universidad Anahuac, the Inter-American Development Bank (IDB), the Mexican Ministry of Economy (SE) and the National Institute of Entrepreneurship (Inadem) was concluded.

New Programs

- **Come to Eat Program:** financing program aimed at restaurants to remodel their facilities, acquire fixed assets and operate their restaurants. 11 loans were granted for a total of 36 million pesos.
- **Financing Program for Broadcasting Business:** financing program for MSMEs Broadcasters, to finance their concession agreements.
- **Program for Gas Stations:** it supports gas stations with financing to make the investments necessary for modernization, facing new conditions of competition in the energy industry.



Alternative Channels

It provides advice to MSMEs and entrepreneurs through the Customer Service Center and the Network of Promoters in the process of affiliation of suppliers to Productive Chain Program and the procedure for obtaining sectoral financing. It also provides training, technical support and expert advice for the operation of electronic products to EPOs and financial intermediaries. In addition, it is developing the venture capital market by investing in innovation and high impact projects through mutual funds and directly.

Portfolio Balances of Private Sector Credit

The total loan portfolio corresponding to the private sector, including guaranteed credit, at the end of December 2016, has increased to a total of 373,475 billion pesos. Of this amount, the Guarantees Program contributed 44%, the traditional credit another 44%, and productive chains the remaining 12%. In accordance with its mission of assisting the country's smallest businesses, 76% of the portfolio balance to the private sector was concentrated on MSMEs.

Business Training and Technical Assistance Program

From January to December 2016, with the Training and Technical Assistance Program and Internships, 126,737 entrepreneurs and/or MSMEs entrepreneurs were served, considering courses given in the Business Development Center (Cedem), mobile office, Consultants Network, e-learning platform and internships.

	Beneficiaries		
	Annual Program 2016	Performed Jan-Dec 16	Progress (%)
Total Trained	100,000	126,737	127
Attending	50,000	56,045	112
On-Line	45,000	51,088	114
Mobile Office	5,000	19,604	392

In addition to their financial activity, Nafin, within the framework of strategies in their Training and Technical Assistance Program, conducted the following actions during 2016:

- ✓ The new facilities of Cedem were inaugurated, providing a better service for the benefit of SMEs.
- ✓ In September, the course "Diagnosis for Micro and Small Enterprises" was implemented in the on-line platform, whose main objective is to obtain a more accurate diagnosis of training and technical assistance needs for micro and small businesses to strengthen their opportunity areas in the administrative process.
- ✓ New entrepreneurial contents of training were added, such as: Strategic Planning, How far I want to go with my company, Basic Accounting for micro and small enterprises and How to present my business project.
- ✓ Courses updated: Regime of Fiscal Incorporation (RIF) How to successfully deal with legal problems of your business and 13 steps to make your business plan.
- ✓ 7th and 8th Corporate Governance workshops were held, with an attendance of 119 people and 54 companies. As of December, 224 companies and 545 people had attended eight workshops, and 368 entrepreneurs attended the Top Conference on Corporate Governance given in March 2016 allowing to implement the pilot project with Fundes/CAF about Corporate Government in 2016. Workshops were evaluated with 93% and 94% satisfaction level, respectively.
- ✓ The Second International Best Practice Program for Development Banks, Nafin Model with the participation of 12 international organizations and 21 participants with a satisfaction level of 95%, and the internship with Colombia's Foreign Trade Bank (Banco de Comercio Exterior de Colombia, or Balcoldex) and Young America's Business Trust were executed.
- ✓ On energy efficiency for SMEs, the second version of the course Economic Evaluation - Financing Project of Energy Efficiency and Renewable Energy was held with 32 participants from various financial intermediaries



and consultants, and in conjunction with the United States Agency for International Development (USAID) the “Guide to Business Plans for Development Projects of Energy Efficiency and Renewable Energy” was developed under the Entrepreneurial Eco Credit Program.

- ✓ The Certification in Project Evaluation was started to strengthen the institutional capacities of Nafin in implementing priority projects and programs.

As regards attention channels, it highlights the following:

- ✓ With the three Nafin Mobile Offices, throughout Mexico 1,166 courses were taught and trained 19,604 beneficiaries.
- ✓ Through Cedem and together with the network of 49 instructors nationwide, 2,732 classroom courses were given, with which 56,045 beneficiaries were trained.
- ✓ From this total amount, 275 courses corresponded to the Regime of Fiscal Incorporation (RIF) with 5,021 people trained.

The on-line platform “Nafintecapacita.com” has 26 courses of entrepreneurial development, with 51,088 active users (cumulative) who have taken 86,482 courses.

Regional Promotion Network

Credit and guarantees granted to the private sector at the end of 2016 amounted to 550,789 billion pesos, supporting a total of 715,741 beneficiaries. By regional classification it highlights the central region with a share of 51%.

Regional Promotion and Institutional Relations Division, as the main sales channel for products and

services of Nafin in the 32 states of the country, carried out the promotion of institutional products and services and supported product managers.

Results from the regional promotion of institutional products and services during 2016 were as follows:

- The base contact of Nafin with SMEs and larger companies in the country was expanded, visiting 1,088 new companies in order to detect their financing needs and make the sale of products and institutional services.
- Nafin is now better known in most states of the country by supporting the design of routes followed by its three mobile offices, manage before local authorities to install them and promote locally the training program in 116 municipalities, some of them visited more than once. Through mobile offices, business training was provided to different segments of the population.
- 70 cooperation agreements were executed with Business Organizations in 27 states.
- 362 interviews were conducted and 355 publications were made in local media.
- Speakers participated at 525 promotional events to disseminate programs and institutional products.
- Derived from this support, 94 projects had access to financing through Credit or Guarantees.

The above activities were aimed at:

- Disseminate information regarding Nafin activities in the states.
- Promote the portfolio of products and services that Nafin has for different business segments.
- Establish local alliances for promoting Nafin products designed to assist SMEs.
- Identify the requirements and needs of business groups and governments in the states.
- Generate business for Nafin with a focus on regional development.



**OPERATION FOR PROMOTION OF PRIVATE SECTOR BY SECOND FLOOR,
FIRST FLOOR AND GUARANTEES REGIONAL CLASSIFICATION**

Millions of MXN-Number of Companies

Credit and Collateral January-December 2015			Credit and Collateral January-December		Percentage Variation 2016/2015		Frame % Amount		Frame % Companies	
Amount	Emp*		Amount	Emp*	Amount	Emp*	J - D 2015	J - D 2016	J - D 2015	J - D 2016
591,533	534,270	TOTAL	550,789	715,741	(6.9)	34.0	100.0	100.0	100.0	100.0
28,704	29,736	NORTHWEST	29,388	42,990	2.4	44.6	4.9	5.3	5.6	6.0
8,595	8,026	B. California Norte	9,139	17,393	6.3	116.7	1.5	1.7	1.5	2.4
2,471	2,243	B. California Sur	1,783	5,946	(27.9)	165.1	0.4	0.3	0.4	0.8
9,901	6,590	Sinaloa	10,721	6,430	8.3	(2.4)	1.7	1.9	1.2	0.9
7,738	12,877	Sonora	7,745	13,221	0.1	2.7	1.3	1.4	2.4	1.8
131,821	67,042	NORTHEAST	105,964	108,201	(19.6)	61.4	22.3	19.2	12.5	15.1
17,087	14,029	Coahuila	14,531	17,785	(15.0)	26.8	2.9	2.6	2.6	2.5
11,952	7,581	Chihuahua	11,056	8,376	(7.5)	10.5	2.0	2.0	1.4	1.2
3,821	5,367	Durango	3,925	13,421	2.7	150.1	0.6	0.7	1.0	1.9
87,760	25,010	Nuevo León	66,599	39,223	(24.1)	56.8	14.8	12.1	4.7	5.5
11,201	15,055	Tamaulipas	9,853	29,396	(12.0)	95.3	1.9	1.8	2.8	4.1
97,586	99,989	CENTER WEST	89,181	126,723	(8.6)	26.7	16.5	16.2	18.7	17.7
5,561	4,255	Aguascalientes	4,831	6,313	(13.1)	48.4	0.9	0.9	0.8	0.9
3,959	3,132	Colima	5,241	3,462	32.4	10.5	0.7	1.0	0.6	0.5
18,380	16,000	Guanajuato	14,794	18,007	(19.5)	12.5	3.1	2.7	3.0	2.5
44,239	26,493	Jalisco	41,261	27,987	(6.7)	5.6	7.5	7.5	5.0	3.9
10,635	20,161	Michoacán	8,729	30,186	(17.9)	49.7	1.8	1.6	3.8	4.2
2,484	3,856	Nayarit	1,852	5,133	(25.5)	33.1	0.4	0.3	0.7	0.7
8,340	21,522	San Luis Potosí	9,378	29,403	12.4	36.6	1.4	1.7	4.0	4.1
3,987	4,570	Zacatecas	3,094	6,232	(22.4)	36.4	0.7	0.6	0.9	0.9
285,526	218,382	CENTER	280,679	290,908	(1.7)	33.2	48.3	51.0	40.9	40.6
181,009	63,126	D.F.	183,261	88,029	1.2	39.4	30.6	33.3	11.8	12.3
3,155	14,167	Guerrero	2,946	32,596	(6.6)	130.1	0.5	0.5	2.7	4.6
8,187	14,149	Hidalgo	6,614	14,064	(19.2)	(0.6)	1.4	1.2	2.6	2.0
59,198	71,797	México	52,322	77,039	(11.6)	7.3	10.0	9.5	13.4	10.8
4,682	12,598	Morelos	7,430	19,518	58.7	54.9	0.8	1.3	2.4	2.7
8,875	6,342	Querétaro	8,720	9,220	(1.7)	45.4	1.5	1.6	1.2	1.3
18,729	30,591	Puebla	17,894	43,764	(4.5)	43.1	3.2	3.2	5.7	6.1
1,691	5,612	Tlaxcala	1,492	6,678	(11.8)	19.0	0.3	0.3	1.1	0.9
47,895	119,121	SOUTH-SOUTHEAST	45,577	146,919	(4.8)	23.3	8.1	8.3	22.3	20.5
6,096	7,101	Campeche	5,242	10,078	(14.0)	41.9	1.0	1.0	1.3	1.4
6,116	20,976	Chiapas	4,516	16,697	(26.2)	(20.4)	1.0	0.8	3.9	2.3
4,694	13,698	Oaxaca	3,053	15,960	(34.9)	16.5	0.8	0.6	2.6	2.2
3,353	11,171	Quintana Roo	3,594	11,745	7.2	5.1	0.6	0.7	2.1	1.6
5,225	9,719	Tabasco	5,740	13,877	9.9	42.8	0.9	1.0	1.8	1.9
16,297	44,615	Veracruz	17,329	64,168	6.3	43.8	2.8	3.1	8.4	9.0
6,114	11,841	Yucatán	6,103	14,394	(0.2)	21.6	1.0	1.1	2.2	2.0

* By millions of People



Advisory Councils

During 2016, the strategic relationship of Nafin with entrepreneurs nationwide was strengthened through Advisory Councils, which additionally have become a benchmark in the Federal Government in terms of relationship with the business sector.

Nafin Advisory Councils have the participation of 659 advisors at national level. It has also increased the participation of women in the Advisory Councils, which is a constant task of gender inclusion, with 88 in 2016.

Regarding the Advisory Councils activity in 2016, 127 sessions were held in the 32 states. The participation that advisors had in five working committees is stressed, which focused on the following topics:

- Design of products according to the regional trends
- Promotion and inclusion of new clients
- Support to entrepreneurs and promotion of innovation
- Training and technical assistance
- Institutional Relations

The operation of five working committees led to the generation of 397 agreements related to the promotion of institutional services and business generation, which have already attended 350 requests, representing an increase of 88%.

Advisory Councils have helped Nafin identifying opportunities for the structuring and instrumentation of programs that boost regional and sector-based economic development, as well as referring new strategic clients of the private sector. Similarly, their contribution has covered areas of opportunity in the public sector through the participation of Economic Development Offices of each state. In addition, they have supported the signing of cooperation agreements with state governments, aimed at implementing programs to support SMEs in these entities as well as strategic programs to promote them.

During 2016, Advisory Councils referred prospects for placing of Nafin products and services, such as: Selective Guarantee, Productive Chains, Treasury Contracts, Entrepreneurs, Empresas Eje (Main Enterprises), Corporate

Financing, Sustainable Projects, Financial Intermediaries, Program of Institutional Market of Corporate Alternative Debt (MIDAS) and customized sector-based programs.

In order to establish business synergies and identify strategies for market penetration and financial support for local businesses, during 2016 the National Meeting of Advisors took place, attended by over 300 advisors and entrepreneurs invited from across the country. This meeting was held in Cancun, QR, and was attended by Nafin General Director and senior management, the state governor, the municipal president of Benito Juárez (Cancun). Works of the meeting were aimed at evaluating institutional programs in each of the regions, holding an open dialog and defining strategies provided by advisors for better execution.

Similarly, board members and other companies participated in Corporate Governance workshops organized by Nafin in Puerto Vallarta and Queretaro. Altogether, it was attended by over 130 entrepreneurs, becoming a forum for discussion and interaction between young and experienced entrepreneurs in Mexico, where work plans for the institutionalization of family businesses were established in order to strengthen the process of succession management.

Credit for Young People

Credit for Young People closed 2016 with a placement of 1,983 credits, which means an injection of 633 million pesos to the Mexican productive sector. Thanks to the significant support and trust of Banamex, Santander, Banregio and Afirme banks, it was possible for 1,274 young people to start a business and the growth and impulse of 794 existing companies.

This initiative, which was presented by the president Enrique Peña Nieto on February 2015, has the purpose of promoting the financial inclusion and economic growth based on access to financing at preferential rates in four different modalities. With the Financial Reform, it is possible to support young people who don't have a credit history and wish to have access to financing services, with amounts from 50,000 to 2.5 million pesos.

In 2016, important events took place after announcing the new age range to apply to Credit for Young People, which



was extended to 35 years, previously having a limit of 30 years old. The objective was to benefit more Mexicans.

Also, it took place Reto Aplicando Mexico, which invites talented young people from across the country to develop the most innovative financial application, with more than 250 projects. In addition, the program Connecting Your Future, a series of training workshops to help young people to discover their talents and materialize business ideas, was launched.

More than 10 cooperation agreements were signed with chambers of commerce, state governments, educational institutions and civil associations in favor of boosting young people and their business initiatives. Promotion was key for positioning the Credit for Young People, with more than 400 conferences where the program was unveiled to more than 48 thousand young people directly, including participation in major events, such as the National Week for Entrepreneurs.

Pyme (SME) Woman

Regarding the program Support for Women Entrepreneurs, which is headed by the Federal Executive Power, 2,715 million pesos were invested in 2016. Note that this program aims to boost business with more than two years of formal operation and are headed by a woman. Thus, thanks to the strong support and confidence of Banamex, Santander, Banregio, Banorte, Affirm and the Mexican Institute of Women, it was possible to support 3,501 companies.



1189 NEW
COMPANIES
IN MEXICO



794
EMPOWERED
COMPANIES

802 MILLIONS OF PESOS DELIVERED



**WOMAN
PYME**

2716 CREDITS
2585 MILLIONS OF PESOS



**WOMAN
RIF**

785 CREDITS
130 MILLIONS OF PESOS

2,715 MILLIONS OF PESOS



INVESTMENT BANKING

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Guarantees on Securities Instruments

Nafin Guarantees on Securities Program continues to encourage businesses to improve their credit rating by issuing debt securities and obtaining more depth in the market, enabling them to place larger amounts for longer terms by accessing a larger segment of investors. The Guarantees on Securities Program is promoted with securities intermediaries, the Mexican Association of Securities Intermediaries and the Mexican Stock Exchange, among others, with the aim of promoting the debt securities market in Mexico.

To date, an intermediary has issued 128 million pesos, 40% of which is guaranteed by Nafin.

Structured Credits

Structured credit provides a specific purpose financing in which companies monetize their asset portfolios, making it possible to isolate operational risk and obtain higher credit ratings, without negative effects on balances. This program

is directed at medium and large companies that generate portfolios with receivables.

Petrochemical Company in Coatzacoalcos

It was authorized in 2012 a loan of 280 million dollars to develop a petrochemical complex in Coatzacoalcos for the production of high and low density polyethylene. The project started its operation (testing stages) during the month of March 2016 and was opened in June 2016.

In addition, this petrochemical project was supported with an authorized credit line in October 2014 in order to finance the Value-Added Tax (VAT) arising from investments made during the Project's period of construction. Currently, the authorized amount of Nafin line is 30 million dollars. In July 2016, a single credit for working capital by 40 million dollars was authorized with a 1-year maturity.

This is one of the most important permanent investments in the last years in Mexico, with more than 5,300 billion dollars. This plant has large regional and national impact and it is an important generator of jobs (about 17,000 in the construction stage). In the operational phase, it will



generate about 2,200 direct jobs and 800 indirect ones. It will also replace approximately 1,500 billion dollars imports annually. The project obtained the Best Projects Awards, awarded by the Engineering News-Record (ENR) magazine as one of the projects of greatest economic and social impact on the world.

Fertilizer Producer in the State of Michoacan

In January 2016, the use of a syndicated loan was concluded, in which Nafin participated with 267.4 million dollars, whose main destination was the acquisition and refinancing of liabilities from a fertilizer plant. This project is a priority for Mexico. It will replace imports and will maintain existing jobs, which is estimated to have more than 2,500 employees.

Mineral Plant in the State of Colima

A credit granted for renewal of an iron ore plant in Colima has been used in accordance with the progress of work. The balance at the end of December amounted to 181.5 million dollars.

Petrochemical Company

Follow up of a corporate unsecured loan is given for 390 million dollars, authorized to rehabilitate and start a fertilizer plant, a priority project for Mexico to replace imports and highly conducive to employment (in the rehabilitation stage more than 800 direct jobs and 1,500 indirect ones.)

Decentralized Public Organization

In September 2016, this organization applied 1 billion pesos, reaching a balance of 2,300 billion pesos, thus using 85% of the authorized line (2,700 billion pesos).

Financial Advisory Services

During 2016, a request for processing expert advice was covered, supporting the placement on the stock

market of Participation Certificates (CPOs). Likewise, in the same period a request for elaboration of technical opinions valuation was covered for Real Estate Participation Certificates (CPI's).

Government Banking

During 2016, Nafin continued to administer loans previously granted to two state-owned companies, Pemex and Comisión Federal de Electricidad (Mexican State-Owned Power Company, CFE) currently State Productive Companies.

Financing of Projects

Pemex Pipeline Project in Central-South Region

Nafin structured this project in conjunction with Banco Nacional de Obras y Servicios Públicos (Banobras, the Mexican State Bank for Works and Public Services,) and participating commercial banks, with a total cost of approximately 1.1 billion dollars. The project has an extension of 290 kilometers, from San Luis Potosi to Guanajuato. The use of resources has been made in accordance with the work schedule project.

Pemex Pipeline in Northern Region

Nafin participates in the North Phase of the System, which will be 453 kilometers long, (from Nuevo Leon to San Luis Potosi). The project will have a cost of 1.518 billion dollars, of which Nafin participates with 240 million dollars. 100% of the credit line has been used.

Sustainable Projects

In line with the objectives of the Federal Government focused on promoting sustainable development in Mexico, reflected in the National Development Plan 2013-2018, Nafin promotes financing schemes and investments from various sources in projects aimed at generating electricity



from renewable sources and clean technologies, to optimize the use of public investment to complement private investment in order to contribute actively in achieving new scopes, responsibilities, investment requirements and expected goals of the energy sector derived from the Energy Reform.

During 2016, the following projects stand out:

Wind Project in the State of Coahuila

In May, two simple loans were formalized to finance: (i) the construction and operation of a wind farm in Coahuila with an installed capacity of 200 MW for a total of 92.9 million dollars, and (ii) VAT derived of the investments required for the construction of the project in the amount of 955 million pesos. Nafin participates in the project as structuring bank, broker and lender.

Wind Farms in the State of Nuevo Leon

In June, two wind farms began operating in Nuevo Leon with a combined installed capacity of 252 MW. Funding granted for its construction and operation amounted to 68.8 million dollars.

Wind Farm in the State of Chiapas

In December, two simple loans were formalized to finance: (i) the construction and operation of a wind farm in Chiapas with an installed capacity of 21 MW for a total of 426 million pesos, and (ii) the VAT arising from investments required for construction of the project for a total of 67 million pesos. Nafin participates in the project as structuring bank and single lender.

Wind Farm in the State of Oaxaca

In December, a refinancing was made by 900 million pesos granted for the development of a Wind Farm with installed capacity of 137.5 MW in Oaxaca. The project is successful running since September 2014.

Small Hydropower Plant in the State of Nayarit

During the month of February, CFE started running the first hydroelectric power plant financed by Nafin, with an installed capacity of 28.8 MW in Nayarit.

Also, on August 2, CFE made its first payment of capital to Nafin, being current in all its payment obligations. During the first half of the year, CFE liquidated its entire VAT credit derived from returns made by Mexico's Internal Revenue Service (SAT).

CFE Productive Chain Supports Mexican Suppliers of Electric Infrastructure in the state of Sonora

In August, a syndicated loan was arranged with commercial banks for the financing of a bid with CFE, in order to carry out the design, construction and commissioning of seven transmission lines with a length of 426 km and five electrical substations associated with the construction of "Empalme I" Central Station in Sonora for 46.2 million dollars. At the close of 2016, there have been five withdrawals.

Wind Farm in the State of Puebla

In August, Nafin dabbled in schemes according to the new environment of the electricity market through the formalization and subsequent disposal of a loan of 1,121 billion pesos to finance costs associated with the construction, operation and commissioning of a wind farm of 66 MW installed capacity in Puebla. Through this project, Nafin starts a relation with the main private producer of electric power in Mexico, and the first wind producer in the world (Iberdrola.)

Hydropower Plant in Puebla

On December 7, Nafin formalized a syndicated credit as structuring bank in favor of a hydroelectric power plant of 36 MW in Puebla, amounting to 400 million pesos to refinance liabilities in USD kept by the company and in



which Nafin participated jointly with commercial banks. On December 15, a withdrawal was held on the credit for the entire authorized amount.

Shared Wholesale Network

During October, the participation of Nafin was authorized in the project for the development of the Shared Wholesale Network (wholesale broadband services network that will market capacity, infrastructure and telecommunications services to dealers and retailers) in the amount of up to 5,500 billion pesos. Funding will be awarded with development bank for a total amount of up to 17,500 billion pesos.

Credits Prepaid

Prepayments of two simple loans granted for the construction and operation of two wind farms in Oaxaca and a photovoltaic solar park in Baja California Sur by 193.9 million pesos, 17.2 million dollars and 25 million pesos, respectively, were received in March, May and June.

Results

In 2016, it has been added to the portfolio of sustainable projects: three wind farms in Coahuila, Puebla and Chiapas; a mini-hydroelectric plant in Puebla; and a project of five electrical substations with 426 km of transmission lines in Sonora. Thus, the presence of Nafin in Mexico and in the energy sector expands.

These transactions represent the opening of new business segments for Investment Banking, through major financing, aimed at developing strategic sectors in the country, which, in alignment to the framework of the Energy Reform, Nafin will contribute to increase the country's transmission infrastructure and electricity coverage.

Investment Programs

Direct Stock Investment

Regarding the permanent portfolio of companies, during 2016, several actions were performed for following up Nafin direct stock investment portfolio:

- We attended the assembly of one company in which Nafin has shareholding, where the reports were released to the Board of Directors as for the activities of the corporations, the financial statements corresponding to 2015 and other matters.
- Capital calls were received by a bilateral fund with Nafin participation.
- There was compliance with the quarterly sending, through SHCP's platform of the IT system, of the financial statements and account statements of Fideicomiso de Apoyo al Mercado Intermedio Valores (Trust Fund for Supporting the Intermediate Market of Securities) FAMIV 9173.

Indirect Stock Investment

Nafin fosters and develops the risk capital industry in Mexico through Corporación Mexicana de Inversiones de Capital, S.A de C.V. (CMIC or Fondo de Fondos (Master Fund).) The corporate structure of CMIC is divided into vehicles with thesis of specific investment in Private Capital, Entrepreneur Capital or Venture Capital, Mezzanine Debt and Energy Sector.

As of December 2016, CMIC keeps a commitment for 896.5 million dollars in 73 investment funds and 16 direct joint investments, supporting 193 Mexican enterprises and more than 61,700 direct jobs.

Also, Nafin participates as shareholder of Banco de Desarrollo de America Latina (CAF,) with an amount equivalent to 1.3% of the regular stock of this multilateral organization. SHCP Minister, Nafin Board of Directors chairman (SHCP Minister), participates as a member of CAF's Board of Directors, in order to promote financial and technical cooperation schemes for the development of SMEs in Mexico.



Programs of Institutional Market for Corporate Alternative Debt (MIDAS)

In order to comply with its mandate efficiently, Nafin has designed an institutional program called Programa Mercado Institucional de Deuda Alternativa Societaria (Program of institutional Market for Corporate Alternative Debt, MIDAS,) which brings together the credit support of Nafin so that companies carry out their modernization and expansion plans, as well as fostering the security market, by encouraging companies so that they, in a term no longer than three years, become candidates to issue debt in the Mexican Stock Exchange (BMV) through the compliance of a program to strengthen its corporate government, in order to provide third parties with transparency and certainty.

From 2105, we continued to promote this Program. To date, 26 companies have been attended, 15 analyzed and five credits have been awarded in an amount equivalent to 2.550 billion pesos. Companies began with a plan to institutionalize its governing bodies to subsequently issue debt in the stock market. It is expected that in the second half of 2017 is placed in the Mexican Stock Market (BMV) the first company promoted by the MIDAS program.



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Project Management

At the close of 2016, the disbursement of resources as a direct borrower of International Financial Institutions (OFI), amounted to 660 million dollars from CAF and 73.4 million dollars from KfW, intended for working capital lines and financing green projects, respectively.

The following programs were supported in the period:

Non-Reimbursable Technical Cooperation granted by IDB ATN/TC-13019-ME for 409 thousand dollars.

On April 1, 2016, IDB approved an increase of 109,878 dollars; reaching a total of 409,877 dollars to fund the program's main activities. On December 13, an extension for the execution of resources was authorized until December 17, 2017. During 2016, 113,853 dollars were disbursed achieving a 70% advance in the use of resources.

Conditional Credit Line for Investment Projects (CCLIP I) with IDB, Loan No. 2226/OC-ME for 100 million dollars, to promote the development of SME suppliers and contractors for Mexico's oil industry and alternative energy projects associated with the oil industry. The balance of the debt at the end of 2016 is 92.5 million dollars.

CCLIP II Line with IDB, Loan 2671/OC-ME for 50 million dollars, to contribute to the efforts of Mexico to increase renewable energy in electricity generation and reduce emissions of greenhouse gases. Funds were disbursed in full on December 24, 2012. During the first half of 2013, the loan's audit was carried out and delivered to IDB a Binder of Audit to Financial Reports with figures as of December 31, 2012. On October 2, 2013, IDB declared "no objection" to the final report of the loan. Finally, at the end of December 2015, 50 million dollars were released, corresponding to the securitization of a wind project financed by this line. It was negotiated with IDB an advance payment of the entire loan line, dated May 12, 2016. IDB approved its acceptance and sent the corresponding collection letter due on June 15, 2016.

CCLIP III Line with IDB Loan 2843/OC-ME for 100 million dollars for the Financing Program of Renewable Energy Projects. On 28 November 2012, the Governing Council authorized Nafin to formalize the legal documentation of this operation. As of December 2014, 36.1 million dollars were spent, using all of the line for 100 million dollars under reimbursement mode. The loan closed in June 2015. During the first quarter of 2015, it took place the closing audit and Ministry of Public Administration (SFP) instructed the application of a contractual penalty to the



auditors firm, same that was accepted and filed on February 24, 2016. However, the payment request for settlement was presented by the auditors firm and carried out by Nafin until July 2016.

Credit line 3237/OC-ME with IDB for 350 million dollars to finance the Program for the Promotion of Cogeneration in Mexico with IDB. The Program consists of a global credit operation that will contribute to the strategic implementation of Nafin in the structuring and funding of sustainable projects, to take advantage of the opportunities that the use of natural gas provides, as well as for the improvement of the transportation network, storage and distribution of gas, by funding the private sector, encouraging and orienting toward a green and inclusive growth and supplying energy at competitive prices, with quality and efficiency all throughout the productive chain. 100 million dollars from this Line were disbursed at the end of December 2016.

Loans and Technical Cooperation of IDB and the Clean Technology Fund (CTF) for the Funding and Transfer Program of Risks for Geothermal Generation. On May 17, 2016, the total eligibility for disbursement operations was obtained, mainly with the presentation of the Program's operating regulations. Currently, the disbursement mechanism of donation for 20 million dollars is prepared for the creation of the fund to cover credit risks granted under the Program, in particular the legal and accounting runway with the participating areas. Currently, the Department of Sustainable Projects, as executing area of the Program, conducts identification, promotion and analysis to generate a portfolio of geothermal projects that can begin arrangements for disbursement during 2017.

KfW line for 31.2 million Euros for the Program of Environmental Improvement in SMEs. As of December 31, 2014, 20.4 million euros of Tranche I were disbursed, consuming all this facility. From this amount, 11.7 million euros correspond to the Program of Small Freighter (Man-Truck,) aimed to fund 164 credits granted by the financial intermediary to beneficiaries that had a junk certificate. The remaining 8.7 million euros were aimed to the Program of Environmental Improvement of SMEs in Mexico, granted by FIDE (Trust for Saving Energy) under the support of the Entrepreneurial Eco Credit Program.

Additionally, Tranche II of this credit line for 10.7 million euros has been spent almost entirely and the balance at the end of the period is 180 thousand euros. SHCP in February 2016 authorized the line's renewal for using these resources during 2016. As for the financial contribution, work was made with KfW, FIDE and the Ministry of Energy (Sener) in the action plan for using the resources of this technical cooperation for Nafin fostering programs and strengthening the Entrepreneurial Eco Credit Program run by FIDE. At the close of 2016, 92 thousand from 1.02 million euros have been provided for consultancy relating to the Small Freighter (Man-Truck) program, with consulting services for the modernization of FIDE's Platform Program, implementation of new functionalities in the Information its System Program, a training plan for all those involved in the Entrepreneurial Eco Credit Program, a consulting to support the International Financial Organizations Division in international recruitment processes, indexing services 20,000 files for FIDE, and the development of a plan to advertise this Program also for FIDE, which represented a disbursement of 570,000 euros. Finally, the available balance of 452,000 euros is aimed to hire a market study to position the program and the acquisition of monitoring, reporting and verification equipment for FIDE. In September 2016, KfW approved a deadline extension for disbursements to November 30, 2017, allowing to use the remaining resources with the contract provided for in the Plan of Action.

KfW Funding line for 53.05 million dollars. On December 2, 2015, this line mainly intended to fund the Program for Energy Efficiency in SMEs (Eco Credit for Energy Efficiency in Enterprises) was formalized. During 2016, 23.4 million dollars were disbursed, leaving an undisbursed balance of 29.7 million dollars, which intends to be used during 2017.

KfW Funding line for 50 million dollars. In February, Nafin accepted a non-binding offer to start negotiations for a line of promotional loan for 50 million dollars for its Program of Renewable Energy Financing. On that occasion, on May 31, both institutions signed a confidentiality agreement in order to share information on projects financed with these resources. They began loan negotiations in September, concluding on December 7 with the signing of the loan agreement. On December 23, the entire loan line to support the financing of a wind farm was disbursed.



Uncommitted line with CAF for 300 million dollars.

On September 26, 2013, the agreement letter was signed, aimed at financing all kinds of operations and free availability of Nafin for: (i) working capital; (ii) foreign trade, working capital and extensions of customer portfolio; (iii) productive chains; (iv) funding of sustainable projects, and (v) other corporate aims in general. The operation terms are established on a case-by-case basis and cannot exceed 360 calendar days, starting from the disbursement day. In 2016, four years of disbursements are met under this line, standing out as the most dynamic with 14 disbursements for an amount of 660 million dollars, becoming one of the main instruments for short-term working capital financing.

Negotiation of New Operations Coming from International Financial Organizations

A negotiation was made with the Department of Energy and Climate Change (DECC) of the United Kingdom and Northern Ireland, for funding 50 million pounds. Regarding this matter, the following may be highlighted:

Capital contribution from Government's Department of Energy and Climate Change (DECC) for up to 50 million pounds to fund an Energy Efficiency Program in SMEs with the participation of Sener, FIDE and IDB. The general objective of the program is to foster and support Mexican SMEs to improve energy efficiency, by providing them with funding to invest in efficient technologies and get consultancy on the way to operate efficiently and reduce carbon emissions. Likewise, it is also aimed to open markets for products of energy efficiency and technologies, to contribute to economic development, by means of reduction on operation costs of SMEs, so they can be more competitive. In March 2015, Sener signed with the British Government a General Memorandum of Understanding (MOU) to collaborate in a Program of Energy Efficiency for SMEs, from which a Cooperation Agreement shall derive, which states the objective and actions of the Promotion and Technical Assistance component. In this sense, after several meetings between Sener, DECC and Nafin to advance with the corresponding MOU in determining the intent and route to continue on receipt of funds by the British Government. Nafin proposed using DECC resources to improve financing conditions to the final borrower of an Energy Efficiency Program in MSMEs (Corporate Eco-Credit, "Individualized" mode). However, and after a long wait by Sener, said Ministry

found that the program was still in an early stage and it was not the right time to commit said resources from the British Government until a potential program is found. Also, Nafin was requested to implement a pilot program that would identify whether there would be sufficient demand for the product, so that in a second stage it was decided to receive international resources.

It should be noted that the implementation of the Program was not subject to the formalization of contributions with DECC. On the contrary, the Program continued structuring and is under operation at the end of the first half of 2016.

Line of Credit for 50 million dollars with the European Investment Bank (EIB.) As part of the strategy to diversify sources of long-term funding in dollars, a financing with EIB was negotiated. In November 2016, EIB conducted a Due Diligence to Nafin and the wind farm intended to fund with contracted resources, with a favorable outcome. EIB requested SHCP its "no objection" to grant a loan to Nafin up to 100 million dollars to finance renewable energy and energy efficiency. On December 22, 2016, SHCP granted a "no objection" to EIB to continue said operation, which will be engaged by Nafin in two tranches, the first for 50 million dollars; leaving open the possibility of a second line for the same amount.

EIB will submit the proposal to its internal committee in early February 2017 in order to be able to share with Nafin the first draft of the loan agreement. The negotiation of terms and conditions and the final management for "No objection" projects to be financed will be conducted in parallel. It is estimated that execution will take place during the first half of 2017.

International Cooperation

Latin American Association of Financial Institutions for Development (Alide)

Nafin participated in the 46th Regular Meeting of the General Assembly and 43rd Meeting of Alide National Coordinators, which was held from 17 to 20 May in Rio de Janeiro, Brazil. The central theme was "Whither Latin America and the Caribbean? Growth, Investment, Financing



and Development Bank,” which was analyzed through four themes: productive transformation for sustainable development; towards developing and expanding markets: domestic, regional and global levels; infrastructure, a new vector of growth and integration as a development stabilizer of Latin American economies.

Montreal Group

Nafin participated in the 5th Annual Meeting of Montreal Group, held in Mumbai, India, from 11 to 13 April. As part of the preparation for the event, we worked with other members of the Montreal Group in topics agreed for the period 2015-2016: Risk Management (Risk Management Division), Green Financing (International Financial Institutions Division), and Innovative Products and Services (Product Development Division).

In the 5th Annual Meeting the Saudi Industrial Development Fund was admitted as a new member of the Montreal Group, and it was established that the topics groups for 2016-2017 are: Green Financing (International Financial Institutions Division), Innovative Products and Services On-line and Digitization (Product Development Division). Similarly, members of the Group agreed to hold a meeting on the sidelines of the annual meeting of the World Bank - International Monetary Fund, with the aim of presenting the document Development Bank's Best Practices on Green Financing for MSMEs, which was prepared by Green Financing team and compiled by an outside consultant.

International Development Funding Club (IDFC)

Nafin participated in the 5th Annual Meeting of IDFC, which took place on October 9 in Washington, DC, United States. Topics included the Mapping of Green Financing Report, annually prepared by IDFC, reviewing the results of an internal survey carried out with the intention of determining actions to be taken by the Club, the topics that will focus the 2016 -2017 work, which are: green financing, sustainable urban development, access to financing with the first “project preparation” and development cooperation theme as well as participation of IDFC in events of UN Habitat III and COP 22.

Institute of International Finance (IIF)

Nafin attended the Annual Meeting of IIF Members, which was held from 6 to 8 October in Washington, DC, United States. At that meeting, high-level speakers were presented who covered a wide range of financial issues including Brexit situation and its impact on the financial sector, financial perspectives from different regions, emerging markets, and monetary policy, among others.

London School of Economics and Political Science (LSE)

In 2015, within the framework of the Dual Year Mexico-United Kingdom, Nafin and LSE signed a Memorandum of Understanding with the aim of exchanging information and knowledge in areas of interest to Nafin and establish mechanisms of cooperation for capacity building in areas of green financing, financial inclusion and SME business development with a gender perspective.

Derived from the above, Nafin and LSE agreed to a research program, lasting three years, which considers the stay of an official of Nafin at LSE facilities from October to December, to attend some postgraduate courses and prepare and publish an article of useful research for the bank.

The first year of the program took place from September 22 to December 9, 2016, and the selected participant focused his research on the topic of green financing and the role development banks can play, using Nafin as a case study.

Green Climate Fund (GCF)

On October, 2015, SHCP acting as National Designated Authority (NDA) before GCF, presented the official nomination of Nafin to start the accreditation process as National Implementing Entity. Nafin expressed NDA its desire to access funds of Readiness Program, which are aimed at strengthening the capacities of Nafin in the accreditation process. SHCP informed GCF its approval and appointed PricewaterhouseCoopers (PwC) to perform this task.



Foreign Trade Bank of Colombia (Bancóldex)

Bancóldex and Nafin maintain a close relationship through IDFC and other areas of exchange. Derived from the relation between both institutions, in November 2015, Bancóldex expressed its interest to carry out an exercise of knowledge exchange with Nafin, since they are in process of restructuring and redefining new institutional strategies. In this regard, in February 2016 an internship was carried out in which three Bancóldex officials visited Nafin to get to know its model and programs, aiming to strengthen its restructuring process, while sharing best practices in various issues. As part of this exchange, Bancóldex invited a representative of Nafin to participate in its International Advisory Committee, which meets annually and convenes international experts to nurture the bank's strategy.

Chatam House

The British research center Chatam House invited Nafin to participate in the "Roundtable for Public Sector Strategy 2016" which was held on 28-29 April in Buckinghamshire. This annual event, held since 2010, aims to bring together public servants from various governments who are working on strategic and innovation issues to share experiences and best practices, with the intention to explore areas of collaboration. The meeting also invited the private sector, academia, and philanthropists. Nafin participated in the panel "Measuring progress and ensuring the delivery of results," in which Nafin experience in green financing was shared, focusing particularly on the issue of the first Green Bonds in Mexico in 2015, and accreditation before GCF. Nafin was the sole representative of Latin America in this event.

German Development Bank (KfW)

Nafin maintains a close relationship with KfW running programs of technical and financial cooperation related to energy efficiency. On June 20, 2016, under the Mexico-Germany Dual Year, Nafin and KfW signed a Memorandum of Understanding to expand collaboration between the two institutions to support their green financing programs.

Similarly, Nafin participated in intergovernmental consultations Mexico-Germany as well as at the "Dialogue on

Climate Change and Sustainable Energy Change", organized by SEMARNAT and the German Embassy in Mexico, within the framework of the Week of Sustainability. In that event, Nafin Sustainable Projects Division and Treasury shared their experience in financing green projects.

Best Practices Program for Development Banking: The Nafinsa Model

With the aim of internationally promoting and position Nafin, its Finance Division, in collaboration with the Technical Coordination and the Administration and Finance Divisions, prepared the "Second International Best Practices Program for Development Banking: The Nafinsa Model." For two and a half days, our governing body shared with senior executives of 13 development banks in Latin America, Europe, Asia, Africa and the Middle East, experience, practices and outstanding programs, while strengthening Nafin relationship with other institutions and expanding areas of international cooperation.

Financial Agent

As of December 31, 2016, the portfolio of Financial Agent is comprised of 19 loans: nine of the International Bank for Reconstruction and Development (IBRD, the original institution of the World Bank), seven of IDB and three of the International Fund for Agricultural Development (IFAD). As for eight donations: six from IBRD and two from IFAD for a total of 4,270 billion dollars.

In 2016, it was concluded the execution (disbursements) of an IFAD loan amounting to 5 million dollars and four donations, three from the World Bank and one from IFAD for a total of 83.5 million dollars. Such operations do not register commissions by Financial Agent because it is not debt, but they represent a reduction in the portfolio of Financial Agent, so that by 2017 expected commissions will not be affected significantly. Also, new operations were contracted.

During 2016, four loans and a donation became official:

- Second Loan to Strengthen Public Finances for 600 million dollars with IDB
- Loan for the Program to take care of Social Backwardness



in Urban Areas and Basic Services for 200 million dollars with IDB

- Loan for Energy Efficiency Project in Municipalities for 100 million dollars with the World Bank
- Loan for the Productive Inclusion Program for 6.5 million dollars with the International Fund for Agricultural Development.
- Donation for Productive Inclusion Program for half a million dollars with IFAD.

Also, seven new operations have been identified, already assigned by SHCP to Nafin as financial agent, according to the following detail:

- Four IDB loans to support Community Education Programs for Basic Education Schools for a tentative amount of 100 million dollars, to be implemented by the National Council for Educational Development, the Program for the Construction and Equipment of the National Center of Animal Health, for a total of 145 million dollars, by the Mexican Service of Food Health, Safety and Quality, the Program of Social Inclusion PROSPERA, for a total of 600 million dollars and the Program to Support Employment, which amount has not yet been defined by SHCP, which will be implemented by the Ministry of Labor and Social Welfare.
- Three loans from the World Bank to support the Intra-Urban Housing Project for a tentative amount of 150 million dollars, to be implemented by the National Housing Commission and a Higher Education Program, for a total of 130 million dollars and the Program to support the National Agricultural Storage System for a total of 120 million dollars.

Derived from the above, attention was provided to 48 preparation and supervision missions of OFI, from which, 14 of them were field visits. Significantly, the visit by World Bank officials to review the results of the Project on Adaptation to Climate Change Impacts on Wetlands in the Gulf of Mexico, which is supported with funds from the TF-

96681 Donation, whose execution ended on October 31, achieving a satisfactory closure despite a significant lag in disbursements. Nafin, in its role as financial agent, worked with the Institute of Water Technology and the Institute of Ecology and Climate Change, providing technical assistance and training in procurement, so recruitment process is taken in accordance with applicable regulations of procurement with foreign credit, agreed between IDB and SFP.

It is also important to mention our participation in the “Workshop on Renewable Energy and Energy Efficiency in the Agricultural Sector,” attended by Sener, the Mexican Institute of Ecology and Climate Change, Agriculture-related Trusts, the Ministry of Agriculture, the World Bank and Nafin, to review issues related to 2016 prospects for adaptation and mitigation of climate change in the sector, synergies with other government agencies on climate change and the results of COP 21, as well as issues of cost reduction in food production and productive sustainability within the Sustainable Rural Development Project financed with loan 8216-MX and TF 93134 Donation.

Finally, as every year, the Working Meeting on Procurement and Financial Management was held by the World Bank with the participation, for the first time, of SHCP, IDB, SFP and other financial actors, in which the following steps to implement the new regulatory framework of the World Bank were agreed, as well as dates to start the negotiation of such regulations with the Mexican government. In this regard, SFP stressed the importance of Nafin participation as a representative of the Ministry of Finance in its capacity as Financial Agent in the negotiation and implementation of agreed documents on external credit.

The main sectors funded by the financial organizations are: energy, agriculture, social, education, environment, climate change and health. Disbursements at 31 December amounted to 1,298,750 trillion dollars, while income from fees charged as Financial Agent amounted to 233 million pesos.



TREASURY AND MARKETS

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Treasury

Funding

In order to ensure that Nafin always has sufficient resources and is able to spread them to different business areas under the best conditions of cost and term, the Treasury shall carry out a funding strategy based on diversification of sources and in performing operations derived from coverage.

Continuing the strategy launched in the last quarter of 2013, during 2016 the Treasury issued Development Banking share certificates through syndicated auction mechanism, which allowed to:

- Improve liquidity conditions.
- Develop the debt curve of the development banking at longer terms by transmitting the benefits of funding the industry.
- Promote the integrated development of the security market and of the national financial system.
- Foster the efficiency of local markets of public debt, seeking at all times to make efficient the process of price discovery.
- Have a larger participation of investors.

- Improve the operating dynamics in the secondary market of these instruments.

As of December 31, 2016, 50,750 billion pesos are outstanding in Nafin Trust Certificates, of which 44,750 billion pesos were issued by syndicated auction, 10,550 billion pesos to three years and revisable interest rate and 34,200 billion pesos in a term of 10 years and fixed interest rate.

As for funding in foreign currency, the main vehicles were the Program of Deposit Certificates of the London Branch, deposit at a certain term of the Promotion Table and the lines of Working Capital.

Cebures - Euroclear

In April 2016, under the scheme of Syndicated Auction, Nafin successfully conducted the first issuance of Development Banking stock certificates settled through Euroclear and Clearstream, thus facilitating public access for the international investor to such debt certificates, which resulted in participation of both domestic and international investors. The amount of the above Bonds amounted to 5 billion pesos.



Additionally, and in order to give continuity to this issue, the respective reopening in the amount of 4,200 billion pesos was made, which also meets the requirements of being payable through Euroclear or Clearstream.

These actions are given under the Operating and Financial Program 2016, which aims to contribute to the economic development of the country to facilitate access to financing for MSMEs and contributing to the development of financial markets.

Green Bond

During August 2016, Nafin made the first issue of a green bonds in Mexican currency. It was the first issue to be listed in the Green Bonds segment of BMV.

This issue marked a watershed in Mexico and later contributed to the promotion of two other issuers, such as the Mexico City International Airport and the Mexico City Government which placed two new green bonds.

With this, Nafin is confirmed as a pioneer in this market in Mexico and fulfills its mandate to develop stock markets in Mexico.

Capital Management

The strategy of minimizing the exposure of Nafin capital to movements in interest rates, with the coverages necessary to protect the income that the bank receives for financial margin, thus complying with the objective of the Treasury of ensuring that capital risks are found within approved limits, being able to strengthen the bank's capital.

Investments

In Mexican currency, there is a fixed term portfolio, mainly with Federal Government bonds, which supports the generation of income. The liquidity portfolio comprised mainly by Governmental securities, and which is used as warranty in the payment systems of Bank of Mexico, as well as by a portfolio of corporate securities that contributes to the private debt market development.

Profit generation through financial margin in US Dollars has come from investment fixed term portfolios, and available for sale: strategic assets which have been maintained as Nafin coverage, by hosting long-term funding lines. Both portfolios are maintained, practically in full, in United Mexican States Bonds (UMS).

As for the liquidity portfolio in foreign currency, and taking advantage of the conditions at the international markets, the main strategy is optimizing profitability of surpluses in US Dollars, by means of synthetic investments in Pesos. Management of liquid resources, however, particularly with development banks, has generated about 20 million pesos in profits.

London Branch

Efforts in promoting and seeking new customers have shown results in the first half of 2016, increasing by 54% its customer base. It is worth mentioning that the work of diversifying our customer base is maintained and in June, we began with the initiative to offer this program to companies.

With regard to the placement and issuance of long-term notes, in the months of May, June and December three 5-year issues were placed in dollars, which improves the maturity profile of liabilities, thereby reducing the gap in Nafin capital with attractive funding costs that distinguish Deposit Certificates (CDs) programs.

The establishment of new partners for CD programs provides the ability to raise funds in foreign currency, which supports the achievement of funding goals by International Treasury and this is reflected in profitable operations for Nafin, thus contributing to maintain a strong financial position and presence in international markets.

Our branches have made a change in technology infrastructure that allows to have better control of the operation with advanced technology, which has provided an optimization of human and material resources, all in full compliance with regulations.



Markets

Market Promotion

The strategy to promote financial markets in 2016 was aimed at achieving the goals of measuring income, creating new business opportunities and increase the portfolio of strategic clients according to the bank's financial products and services, based on:

- Reviving investment contracts that boosted fundraising.
- A significant increase in the trading volume of buying and selling securities (revisable instruments, bonds and corporate papers), derived primarily from getting closer and promotion with institutional clients.
- Increase in raising funds in foreign currency (USD).
- Active advocacy in the syndicated auction and green bond programs.

Regarding compliance with the general provisions applicable to financial institutions and other bodies providing investment services, strict compliance, follow-up and monitoring was maintained in operating and promotional activities with customers to whom said provisions apply.

Financial Markets

The sharp drop in oil prices and the Chinese stock market, expectations of rate hikes from the Fed, the Brexit and presidential elections in the United States were the most important events that shaped the behavior of financial markets in the world during 2016.

As noted by Bank of Mexico, in early 2016 prices of riskier assets were drastically reduced, while emerging markets experienced strong net capital outflows due to increased risk aversion, to fears about the solvency of European banks, worsening the prospects of profits for the corporate sector, falling prices of raw materials and doubts about the effectiveness of monetary policy implemented in the major advanced economies to support their recovery. Volatility is remarkably increased.

However, markets began to exhibit greater stability and financial conditions to improve from mid-February after China's efforts to boost growth and stabilize its exchange

rate, and above mentioned responses from major banks. Oil prices touched lowest levels between late January and early February at a price around 26 dollars per barrel (dpb), ascending from there to finish between 53 and 55 dpb, which represented increases of over 100%.

By midyear, the Brexit generated another episode of volatility. After knowing the result of the referendum to remain or not in the European Union, a speculative mood was generated in relation to the next steps that would take the UK government, as well as the impact this decision will have on their future and that of the European Union.

Finally, another moment of volatility was present in the days before and after the presidential elections in the United States, which Hillary Clinton arrived with apparent advantage, but eventually gave as victor Donald Trump. Stock markets in that country reacted positively, while in the debt market rises were presented at interest rates in anticipation of significant increases in public spending and tax cuts. This would give an additional boost to the US economy, but will also exert pressures on inflation.

Money Market and Bonds

At the beginning of 2016 the bond market started strong, showing a remarkable low to mid-2016. At that time the target rate of Banco de Mexico stood at 3.75% until June 29. With the effect of Brexit pressure on the exchange rate prompted the central bank to increase its target interest rate by 50 bp; starting from that moment with an upward cycle of interest rates.

In addition to this, we had presidential elections in the United States with comments by candidate Trump, which began to exert pressure on the exchange rate, prompting a further increase in interest rates, having started the year at 3.25% and closing 2016 at 5.75%.

All this affected significantly the entire bond curve where we saw average increases of 175 bp. In real rate instruments the move was contrary showing average low rates of 50 bp for short-term bonds, basically affected by higher expected inflation. As for middle- and long-term bonds, they showed a slight decrease.



Foreign Exchange Market

The peso-dollar correlation and international oil prices (especially the West Texas Intermediate), remained at high levels, reacting more aggressively to falls in energy prices. Although Mexico is a country that has reduced its dependence on oil exports, reductions are related to lower tax revenues, plus low oil prices postpone oil investment projects not considered profitable. Importantly, emerging countries linked to commodities have had a behavior similar to that of Mexico.

Another important factor to consider is the expected rate hike by the Fed. Many analysts believe that there should be at least one more increase in the year. This scenario would generate volatility in the exchange rate depreciation trend.

Given the “fix” exchange rate of Banco de Mexico, the peso-dollar exchange rate ended 2015 at 17.2487 with a maximum of 19.1754 on 11 February and a minimum of 17.1767 pesos per dollar on April 29, 2016. Throughout the first half of the year, the performance of the exchange rate was volatile, with a depreciation tendency after April as a result of reductions in energy prices, solid US data pointing to a hike in reference rates and UK referendum, which resulted in favor of a way out of this country from the European Union. It should be noted that during the period of greatest pressure, not massive capital outflows from the Mexican markets were presented.

Capital Markets

At the beginning of 2016, Mexican Consumer Price Index (CPI) registered a high volatility due to a sudden increase in risk aversion, which led the main indicator of the Mexican Stock Exchange to show losses higher than -6.0% in mid-January. CPI went on to break its 40 thousand same-day threshold, since it was negatively influenced by a sharp drop in oil prices, which reached valuation levels not seen in the last 15 years. However, the international stock markets quickly recovered thanks to the perception that China’s economy had stabilized and also that several economic indicators in the United States showed a healthy and sustainable growth. In late June, the factor that had the most influence on the markets was the exit of Great Britain from the European Union. The so-called “Brexit”,

led to a massive outflow of investments in England and Europe. This, however, had no significant effect on our local stock market.

In August, CPI recorded its highest level ever reaching almost 49,000 units, supported by extremely positive quarterly reports with significant growth in sales and margin expansion. The devaluation of the exchange rate was a factor that benefited most Mexican companies listed, as together about half of its revenues come from abroad. Likewise, domestic consumption remained strong thanks to the growth of consumer credit, higher real wages and strong remittance flows.

However, from November 8 the outlook for Mexico changed dramatically with the victory of Donald Trump for the presidency of the United States. Warnings of a possible cancellation of the Free Trade Agreement and threats to companies to stop building plants in Mexico had a very negative impact on the exchange rate and prices of shares. The Mexican peso stood above 20 pesos per dollar, while CPI fell more than 4,000 points, reaching 44,000 units in mid-November. By December, the Mexican stock market stabilized and could end the year in positive territory, achieving a gain of 6.2% during 2016 to finish the year at the level of 45,642 points.

In 2016, Capital Markets again achieved a better performance than that recorded by CPI, to achieve a gross return on invested capital of 15.5% versus a yield of 6.2% by the stock market. With the above, net profits of 18.4 million pesos were obtained from funding costs and commissions to brokerage firms.

Derivatives Market

During the period, Derivatives significantly supported Nafin goals along three lines of action. The development of financial markets has become as a market maker in the MexDer derivatives stock for exchange-traded futures of government bonds and CPI. In risk management, operations substantially increased to run more than 120 hedges that protect the income the bank receives on account of net interest income. And, in income generation, trading and arbitrage operations behaved in accordance with goals set earlier this year.



Investment Funds

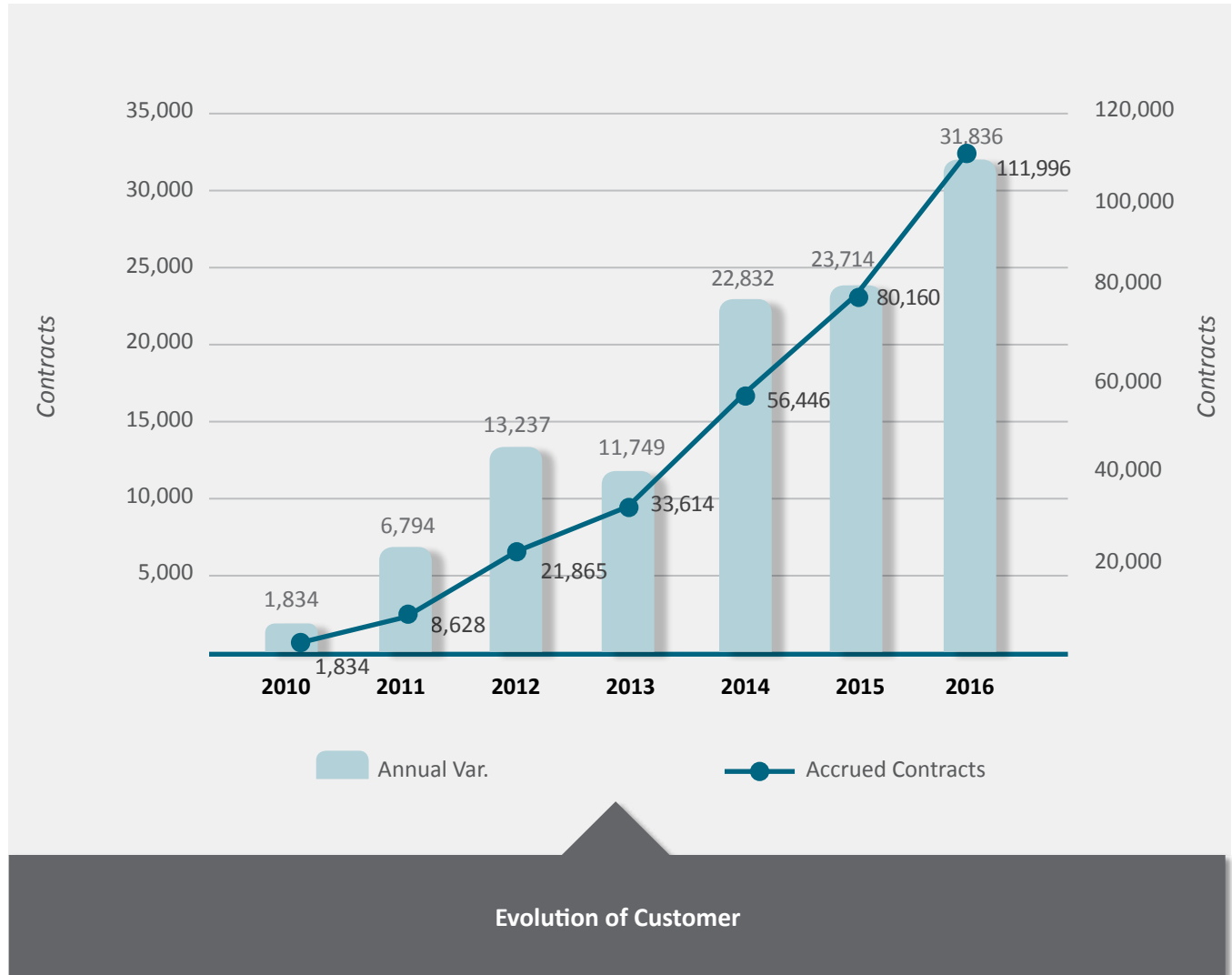
Nafin Fund Operator continued working on fostering access to the security market of small and medium investors, through stock distribution of its 11 funds, with 32 agreements signed with 25 commercial brands in the stock market.

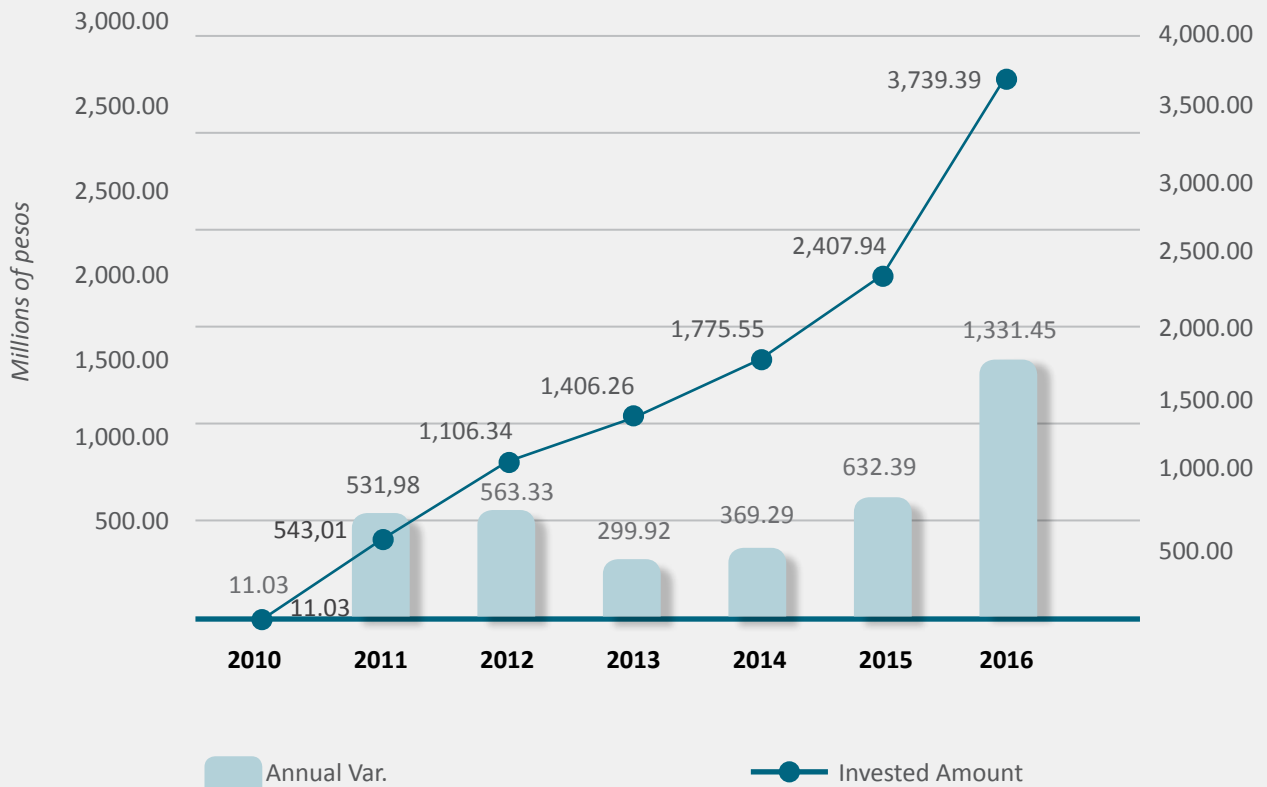
However, the fact that some of our major dealers created their own investment funds, as well as the volatility presented in markets during 2016, provoked that the average assets managed by Operadora de Fondos Nafinsa decreased 28.4% from 30.886 billion pesos in 2015 to 22,097 billion pesos in 2016.

Cetesdirecto (investment in Mexican treasury bonds -CETES- made easy)

During 2016, continuity was given to positioning Cetesdirecto, which is mandated by the Federal Government, through an outreach campaign on social networks and several electronic, print and urban communication media. Also, the use of Apps for mobile devices with iOS and Android operating systems was promoted, which allow the public to access easily and securely to "cetesdirecto." Similarly, a permanent presence in Mexico City's Interactive Museum of Economics (MIDE) and KidZania entertainment center has been maintained as well as in various exhibitions in Mexico.

All of this allowed 2016 to be the best year of Cetesdirecto performance, reaching more than 215 thousand registered customers, of which more than 111 thousand have already invested, reaching more than 3,739 million pesos, surpassing the goals set for the year. Similarly, the total amount of debt placed by the Federal Government in 2016 through Cetesdirecto was 0.73%, outperforming its stake by 49% over the previous year.





Evolution of Amount Invested by



LEGAL AND FIDUCIARY OPERATIONS

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Corporate and Business

Its objective has been to give certainty to legal processes involved in granting credit, financial and risk capital markets, and international and advisory matters. Also, assistance was given to various departments of Nafin in preparing and reviewing contracts for domestic and foreign operations.

The legal activities led to some important results, including the following: the implementation of Nafin's syndicated auctions, with the placement of 22 billion pesos; participation in the formalization of issuances; implementation of updates to the Program for Direct Sale of Certificates to the Public, including consultation and review of legal instruments required by authorities, other entities in the financial sector, customers and service providers; preparing advices for financial authorities in compliance with applicable provisions, updates and services corresponding to the Securities Debt Support Program.

The review, negotiation, validation and updating of framework contracts for Purchase-sale of Securities, Repurchase Agreements, Securities Lending Agreements and Bank Deposit Securities in Administration and Trade

Commission Agreements were also carried out. Additionally, framework contracts for Derivative Financial Instruments, ISDAS (International Swaps Dealers Association Master Agreement,) were executed with various local and foreign financial institutions. Legal advice was provided in the audits performed by different authorities.

Legal advisory services were provided, together with support for implementing the Secondary Market Auctions Program (Subasec) to promote liquidity in corporate and government debt securities, including hiring activities with intermediary participants and brokerage firms that provide negotiation systems.

Legal advisory services were offered for the instrumentation and implementation of the Green Bond issuance in international markets according to Rule 144 and Regulation S, under the U.S. Securities Act of 1933 and the reopening of the issue; the first issue of Green Bonds in Mexico in pesos.

Legal assistance was given to business schemes and advisory services in corporate banking, operations of Financial Agent and financing with international elements that Nafin grants or expects to receive, as well as Holding



Deposit and Collateral contracts to formalize guarantees, credit lines and discounts granted by Nafin through proper departments and the drafting of instruments for Nafin operations as Federal Government's Financial Agent.

Legal advisory services have been provided to prepare the documents necessary for Nafin participation in several corporate financings, as well as energy and petrochemical projects.

As a result of the new businesses initiated by Nafin, it has been necessary to create legal instruments for developing corporate business schemes, which have allowed to participate in syndicated loans and to grant financing to projects for generating wind energy, hydroelectric power generation and provide funding for other alternative energy projects.

Legal support for the formalization of a loan granted under the Program of Institutional Market of Corporate Alternative Debt (MIDAS) was provided.

Nafin has also signed cooperative agreements with various institutions such as the Mexican Chamber of Industry (Canacintra), Pemex, Mexican Fund for Tourism Development (Fonatur) and Mexican Confederation of Business Owners (Coparmex.) Loans have been allocated from Nafin to Pemex, Rural Finance and the National Fund Institute for Workers' Expenditures (Infonacot), among other important operations.

Revision and negotiation of loans and donations financing granted by International Financial Entities among which the Entrepreneurial Eco Credit Program stands out.

Legal advisory is provided to the Entrepreneur Capital Trust Fund to formalize awarded funds of the Inadem tenders.

Governmental Regulations

Acquisitions and Movables:

Nafin properly complied with the government regulations applicable to its nature of being a Mexican Bank,

observing the preparation of legal instruments to achieve the proper development of activities of its various divisions, serving a total of 487 cases under to the following:

- 198 legal instruments were developed.
- 139 reviews of bond policies.
- 18 revisions of bid award process.
- Attention of 16 sessions of Nafin Acquisitions, Leases and Services Committee (CAAS).

Link to the Superior Audit of the Federation (ASF):

Regarding the functions that this division has as liaison before ASF, it is reported that all the information requirements were timely answered and the preliminary and final results presentation meetings of four audits of the 2015 Public Account were attended.

Federal Law of Transparency and Access to Public Government Information (LFTAIPG), Federal Law of Transparency and Access to Public Information (LFTAIP) and the General Law of Transparency and Access to Public Information (LGTAIP)

During 2016, we worked in coordination with Nafin's administrative units (AU) in order to keep updated the information published on the Transparency Obligations Portal in accordance with applicable regulations. So for actions to load information into the Portal System of Transparency Obligations of the Mexican Platform for Transparency (PNT), derived from the entry into force of the General Law of Transparency and Access to Public Information, various actions were carried out, such as: assigning passwords to PNT for various AUs; registry of AU responsible for generating the information; assigning formats consistent with the role of each responsible AU and Support and advice to users responsible for each UA for loading information.

As for Requests for Access to Public Information and Personal Data, during 2016 we received a total of 1,465 requests. The most frequent topic refers to the results of Nafin's primary activities, as well as trust funds and services hired. From responses to said requests received and attended



in 2016, individuals filed before the National Institute of Transparency, Access to Information and Protection of Personal Data (INAI) 14 review resources.

In compliance with the provisions of the Federal Law of Transparency and Access to Public Government Information, in the General Law of Transparency and Access to Public Information and the Federal Law of Transparency and Access to Public Information, it was updated the System of Reserved Records Index, ensuring that information reported by each administrative area was correct.

Legal and Collecting Disputes and Credit Department

This year the commitment to promote and direct legal actions that contribute to achieving the objectives of Nafin as a development banking was ratified, in line with the applicable legal regulatory framework, by providing legal services, recovery of the disputed portfolio, and the design of legal defense strategies for preventing or minimizing economic impacts.

It has thus been possible to diminish the amount of disputed portfolio and contingencies derived from legal proceedings brought against Nafin, reduce accounting provisions and apply said resources to projects with economic and social impact.

In banking formalization services, we have actively worked with business areas to continue promoting the creation of new business schemes and legal instruments that meet market needs to strengthen the development of SMEs and support for Financial Intermediaries. In addition to participation in the development of three new schemes, during 2016 we received and attended 460 requests for formalization of banking operations, opinions of politically exposed individuals and opinions of legal existence of corporations and a summary of faculties.

Also, continuity has been successfully provided to the coordination of a single point of entry to legal services in

relation to banking formalization, as the front office for our Legal Disputes and Credit, Corporate and Business Legal, and Fiduciary Divisions, in relation to Nafin business areas.

Fiduciary Operations

At the close of 2016, the Trust Division manages 459 business, whose trust assets amounted to 1.17 trillion pesos, an amount that represents an increase of 5% compared to the end of 2015 and maintains Nafin as Mexico's second fiduciary institution in the trust market, accounting for 16% of total assets in trust and more than 70% of total assets managed by the development bank.

From the patrimony managed, 288,000 billion pesos (25%) correspond to liquid resources in trusts, of which 124,000 billion pesos are invested in Nafin Money Desk and 8,000 billion pesos in Operadora de Fondos Nafinsa, meaning a 12% increase in the liquid investment of fiduciary businesses, when compared to last year. Of the remaining resources, 54,000 billion pesos are deposited in the Treasury of the Federation and 102,000 billion pesos with other financial intermediaries.

During 2016, actions to strengthen internal control of fiduciary process, highlighting the redesign of the Trust website, updating the fiduciary process and adequacy of the functional structure were made, in addition to continuing purification of business inventory by extinction of 24 trusts that served their purposes and the creation of four to contribute 1.2 million pesos in annual trust revenues by 2017.

In 2016, net income generated by trust activities amounted to 192.8 million pesos, consisting of 189 in fees for trust services and 3.8 in commissions for custody and administration of securities and cash, as well as consulting fees.

With regard to the custody and management of securities and cash, total assets under custody as of December 31, 2016 reached 148,000 billion pesos; this is 9% higher from that at the end of 2015.

SUPPORT TO OPERATIONS

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Quality Management and Organizational Culture

With the goal of maintaining its dynamic of growth and qualitative changes, Nafin maintains its strategy of ongoing improvement in its Quality Management System, in developing human capital, in strengthening risk management, and in the incorporation of an appropriate system in its technological platform for the efficient operation of its programs.

Quality Management System (QMS)

Since its creation in 2001, QMS has successfully incorporated regulatory elements from different authorities aligning them with institutional goals. Today, we have a robust system which regulates the operation of substantive and support processes, by clearly defining the different actors and service levels based on a model of continuous improvement. The success of this implementation is due to the fact that process owners identify and propose improvement actions as a result of their daily operation in Operating Quality Committees.

With 16 years of operation, Nafin Quality Management System has been consolidated as an ongoing tool for analysis, evaluation and improvement of processes. It has been useful to develop and cover regulatory elements and institutional observance, including the Internal Control Model, operational risk management, and compliance with the various programs implemented by SHCP and the Ministry of Public Function (SFP), including the Program for Accessible, Modern Government (PGCM.)

In September 2016, an external quality audit was conducted; therefore, Nafin got an extension of its certificate of compliance with stipulations in Standard ISO9001:2008 for another year.

Quality Operating Committees (QOC)

One of the most important elements within the administration of QMS is the involvement of staff in self-management of their processes' quality, where the outcome of the process operation is evaluated and if it detects deviations or suggest improvements, these are evaluated based on compliance with corporate goals. As of December 2016, 38 QOCs were installed which held session at least one time during the quarter.



Human Capital Development

Talent Detection and Gender Equity

Nafin has a model for managing human capital that is based on the development of competencies and the ongoing evaluation of personnel's potential. This made it possible to cover 45.5% of vacant positions during 2016 with personnel already working in Nafin, thereby reducing recruitment costs and optimizing investment. Also, vacant positions were covered in accordance with public policies corresponding to government programs and designed to promote gender equity, gaining the promotion 44.2% women during 2016.

Also, there is a program to promote the development of talented young people, through professional practical experience and social service. As a result, 32 people for ongoing positions were hired, representing 22% of those hired during 2016.

Moreover, with the firm intention to strengthen the detection of talent, in June 2016 started the implementation of an on-line service, which will identify external and internal staff with skills required for the performance of his/her job, as well as vacancies generated through a methodology to align workforce needs with ours through the generation of a skill-based development model, talent identification, definition of key positions and their replacements, establishing an individual development plan and the operation of internal backups of vacancies.

Priority Training Programs

In 2016, the Training Program was characterized by strengthening the expertise of the divisions that make up Nafin, various actions to benefit as many employees as possible were carried out, such as a Diploma in Business Administration and Finance with the participation of 30 people. In addition, continuity was given to the English Learning Program, with expertise in Business, benefiting more than 100 employees. In addition, specialized training for staff of state offices through an on-line diploma course.

In addition to this, various actions were taken for the staff requiring to certify or recertify courses in accordance with the regulations of their respective areas. Courses with specific agendas and tailor-made for applicants to improve their functions were developed and thus having a positive impact on Nafin.

Internal Comptroller's Office

In situ checks were carried out of various Control Routine Agenda (ARC), the main critical processes and some administrative ones, proving their effectiveness by matching the document and electronic evidence generated from each process execution, presenting the results to the heads of AUs from 43 visits made.

Likewise, and in accordance with Article 164, last paragraph of the General Provisions Applicable to Credit Institutions, it was reported in writing about the performance of the activities referred therein, and the operation of Internal Control System as a whole to the Audit Committee on 18 November and to the Board on December 15, respectively.

Self-control Tools

In the search of best corporate practices, Corporate Control Guides (GCC) were reviewed and redesigned from five Internal Control standards set out in the Committee of Sponsoring Organizations of the Treadway Commission model adopted by SFP.

In November 2016, GCCs were applied so the Heads of the 33 AUs that make up the structure of Nafin will conduct an annual self-assessment exercise on infrastructure of Internal Control, in order to verify the mechanisms implemented, identify potential weaknesses, and where appropriate, establish additional strengthening measures.

At the close of 2016, the universe of self-management tools was composed as follows: **33** Corporate Control Guide, **226** Agendas of Operational Control Routines, and **36** Agendas of Control Routines through which delivery is monitored of timely regulatory reporting.



In addition, during the year incidences of detected Internal Control were generated through activation of control alerts, which in general were lower and of operational type, leaving its registration in the Management System of Internal Control (SACI), being served on average in 1.84 days.

Objectives and Guidelines of the Institutional Model of Internal Control

In October 2016, the Governing Council approved the updating of Objectives and Guidelines of the Institutional Model of Internal Control incorporating the following changes of a substantive nature and form:

- a) General considerations since Nafin is a state-owned organization which meets the provisions of the Internal Control and Risk Management as a Development Bank.
- b) To define powers and responsibilities of AUs for Internal Control.
- c) To specify the characteristics of controls to be implemented.
- d) To specify reporting mechanisms, monitoring, supervision and continuous improvement of mandatory compliance.

Regulatory Reporting and Reports to Authorities

Also, among the activities of Internal Comptroller Division are monitoring the timely compliance in accordance with regulations, regarding information, processing and delivery to the authorities of various reports requested to Nafin.

At the close of 2016, the Internal Comptroller summoned area divisions to start updating reporting inventory and disclosure requirements, which is housed in SACI and thus promote timely compliance. There is an inventory of **366 regulatory reports** requested by various bodies.

Qualification Processes on the Degree of Risk Posed by a Customer

In the period October to December 2016, the Compliance Division attended 202 requests of risk rating in business areas, both from new customers and those already registered for update.

Among the various applications of risk rating, 401 Formats and Know Your Customer ID or User (FICC) were treated; 55 Verification Formats of Politically Exposed Persons; 78 Appendices requests of FICC; 53 requirements of ABC or ABCD Formats, and 66 Honesty formats. 18,283 people who signed the Program of sale of securities directly to the public "cetesdirecto" were checked, without any adverse outcome or motivate a report to competent authorities.

Technological Developments in the Monitoring System for the Prevention of Operations with Illegal Origin and Terrorist Financing

Regarding the work plan of the Implementation of SHCP Best Practices Guidelines technological project at the end of the fourth quarter of 2016, IT concluded the last phase of the Work Program established for this development and successfully checked the functionality of these screens: Information Intelligence Service for the tracking of Lists of Blocked Persons and Generating Unusual Reports Round the Clock and Unusual Ones, pending minor adaptations for generating these reports, which will be held in January 2017.

Training Program on the Prevention of Illegal Operations

In July, the Training Program on Prevention of Money Laundering and Financing of Terrorism was concluded, with the active participation of employees and officers; enrolling a total of 907 people in three types of courses, according to their functions in the position they play:

- General course: 567
- Advanced course: 315
- Specialized Course: 25



Moreover, training courses were held on Prevention of Money Laundering and Terrorist Financing in one-month periods each to staff that started working in the same month, as set forth by internal policies.

Implementation of Processes Aimed at Implementing FATCA

In August, the period specified by SAT to report under the guidelines of Annex 25 of the Tax Miscellaneous Resolution, which refers to give attention to Foreign Account Tax Compliance Act concluded for the first report of new customers and existing individuals, as well as new and existing corporations.

Nafin fulfilled on time the sending of three reports to SAT, according to their specifications.

Internal Auditing

This Division developed and attended its Annual Work Program 2016, which was aimed at the practice of audits on substantive activities, highlighting those related to credits, financial markets, trust and risk management, in which a general objective was verifying compliance with the regulations, among other, established by the National Banking and Securities Commission (CNBV) and Banco de Mexico; evaluate the quality, adequacy and timeliness of financial information; manage risks inherent in processes; and strengthen the internal control system.

According to the above, the activities of Internal Auditing covered the following aspects:

1. Audits

15 audits were conducted, of which six were regulations in accordance with the following: i) Four for credit processes in four stages, ii) one of Risk Management; in compliance with the provisions issued by CNBV, and iii) the operation of Financial-Derivatives Instruments according to the standards of Bank of Mexico; the remaining nine, are as follows: one to the Calculation of Index Capitalization, another to the Financial Agent, the General Cashier and two more to Trusts.

During the development of reviews there was interaction with audited divisions in order to inform the responsible parties the results and added-value proposals that allow addressing remarks, as well as recommendations determined to strengthen the Internal Control System.

2. Auditing Committee

Internal Audit supports the activities of the Audit Committee, among which are to provide the information necessary to report the Board about conditions under which the Internal Control System operates as well as the logistics of meetings, obtaining information for development and monitoring of agreements. In 2016, 10 ordinary and extraordinary sessions were held.

3. Participation as Regulatory Advisors in Decision-making Bodies (committees) Meetings

In accordance with regulatory provisions, we participated in meetings held by the Risk Integral Management Committee and the Communication and Control Committee. Additionally, we participated in the Executive Credit Committee of the Board, the Internal Credit Committee, and from November in the Credit Committee.

4. Monthly Review of Variations in our Financial Statements

In order to assess the reasonableness of the Balance Sheet and Income Statement, monthly, the divisions that present the main changes are identified, making comparative balances of previous financial reporting from the previous month against the preliminary figures recorded in the Financial Information System of the month, determining increases and decreases of balances, and analyzing the origin of variations.

In addition, Internal Audit participated quarterly in the working group with members of the Audit Committee and representatives of the Administration and Finance



Division, for the purpose of carrying out data analysis of Financial Statements and, if necessary, explanations and/or clarifications were made.

5. Audit Management System

During the second half of 2016, use cases (requirements and descriptive screens) were developed and on October 20, 2016, the development initiative of the Audit Management System was presented to the Committee for Systems Planning and Evaluation (COPYES), which was approved.

At year-end 2016, it is in the process of formalizing the Full Range and Functional Requirements (Use Cases and traceability Matrix for each functional requirement and testing protocol), which will be developed with the support of IT.

IT

Continuous Improvement in the Operation

- **Implementation of Video Collaboration Room (Lync Room System) for virtual meetings and on-line collaboration.**

A video collaboration room (Lync Room System) for meetings at least weekly with regional directors and state representatives was implemented and is also used by general divisions in order to serve its customers or suppliers. This project has allowed savings on travel allowance and increased productivity on timely decision-making.

Applied Developments

During 2016, 44 business projects were carried out, which implementation in 25 of them was made through recruitment and administration of external suppliers according to regulations, 4 through a combination of internal developments and hiring and managing external suppliers, and 15 through internal developments that

enabled significant savings, having as benefit not to create a dependency with a supplier. It is important to mention that this strategy allows knowledge and experience to stay and reduces response time to meet business needs, supporting the professional growth of participants in these projects.

From 15 internal developments implemented this year, the following stand out:

- **Internal Control Management System (SACI) Ver. 15.0**

This project involved the generation of reports with export option to Excel or flat file, in order to manage and extract the necessary information in a timely and accurate way for the preparation of executive reports and the adequacy of existing ones to include more criteria, change order and give the option to export to Excel or flat file. Also, it features the adaptation to emails issued by the application to include dates. This development would have generated an expenditure of at least 521,700 pesos.

- **Guarantees and Loans Management System (GESOL) Ver 15**

This project was developed using the Loans Process (PDC) system as reference, for the management and follow-up of First-Tier, Second-Tier and guarantees loans applications, controlling its status in five loans process stages (Promotion, Analysis and Decision, Formalization, Release and Withdrawal) benefiting from available and timely decision-making information for senior management, indicating the stage where each application is with a single source of information. Should we have hired an outside vendor for this development, it would have generated expenditures for at least 582,400 pesos.

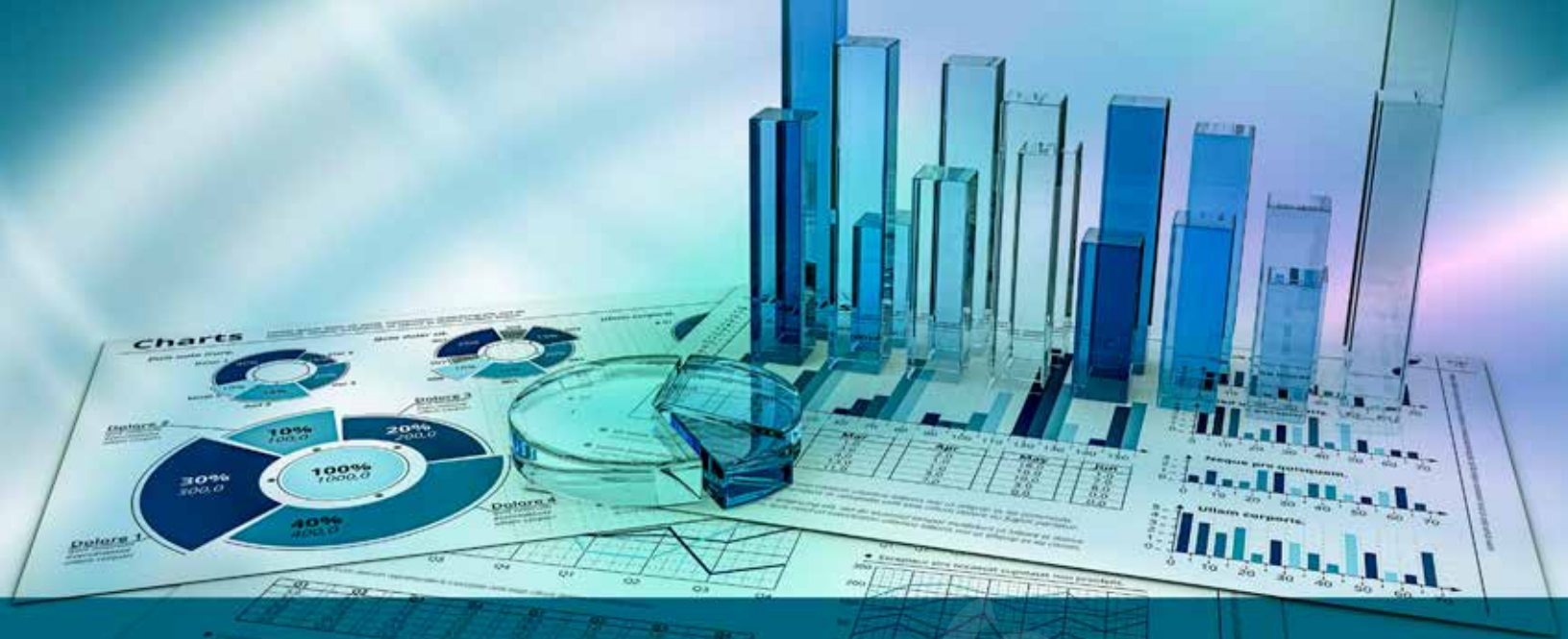
- **Datamart for Liquidity Analysis**

A data model was prepared for implementing this project that allows consolidating and using the information required to analyze, monitor, control and follow-up liquidity risks associated to NafinSA capital, fulfilling CNBV regulatory requirements in risk matters. Should this development had been hired, it would have generated expenses for 700 thousand dollars plus an annual maintenance cost of 142 thousand dollars.



- **Equipment and Furniture Inventory System–SIME Ver. 15.0**

This project consisted in the analysis, development and implementation of the registration, management and control of the information associated to the inventory of furniture and equipment property of Nafin using this programming tools according to institutional standards for IT. The implementation of this project was carried out successfully and implemented with internal resources, which allowed savings of at least 1,829, 120 pesos.



FINANCIAL RESULTS

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Despite the uncertain context and diminishing economic activity, Nafin got a net profit of 1,321 million pesos, equivalent to a 5.2% nominal return on capital during 2016. This way, the equity capital amounted to a total for the end of the year of 26,710 million pesos, representing 10.8% nominal growth against the total revenue of the previous year. It is worth mentioning that the Federal Government used resources from Nafin this year for 800 million pesos. Otherwise, net income would have been 1,801 million pesos and return on equity of 7.1%.

In addition, the bank's financial situation demonstrates solid indicators, including the following:

Indicator	Dec 2015	Dec 2016
Overdue accounts / Portfolio at risk	11 %	1.0 %
Reserves / overdue accounts	211.2 %	205.0 %
Financing granted to MSMEs / Financing to Private Sector	82.4 %	76.8 %
Financial Penetration (Private Sector Accounts /GDP) 1/	1.69 %	1.80 %

1/ Mexican National Geographic and Statistics Institute (INEGI), Preliminary figures as of 4th Quarter 2016, published in February 2017.

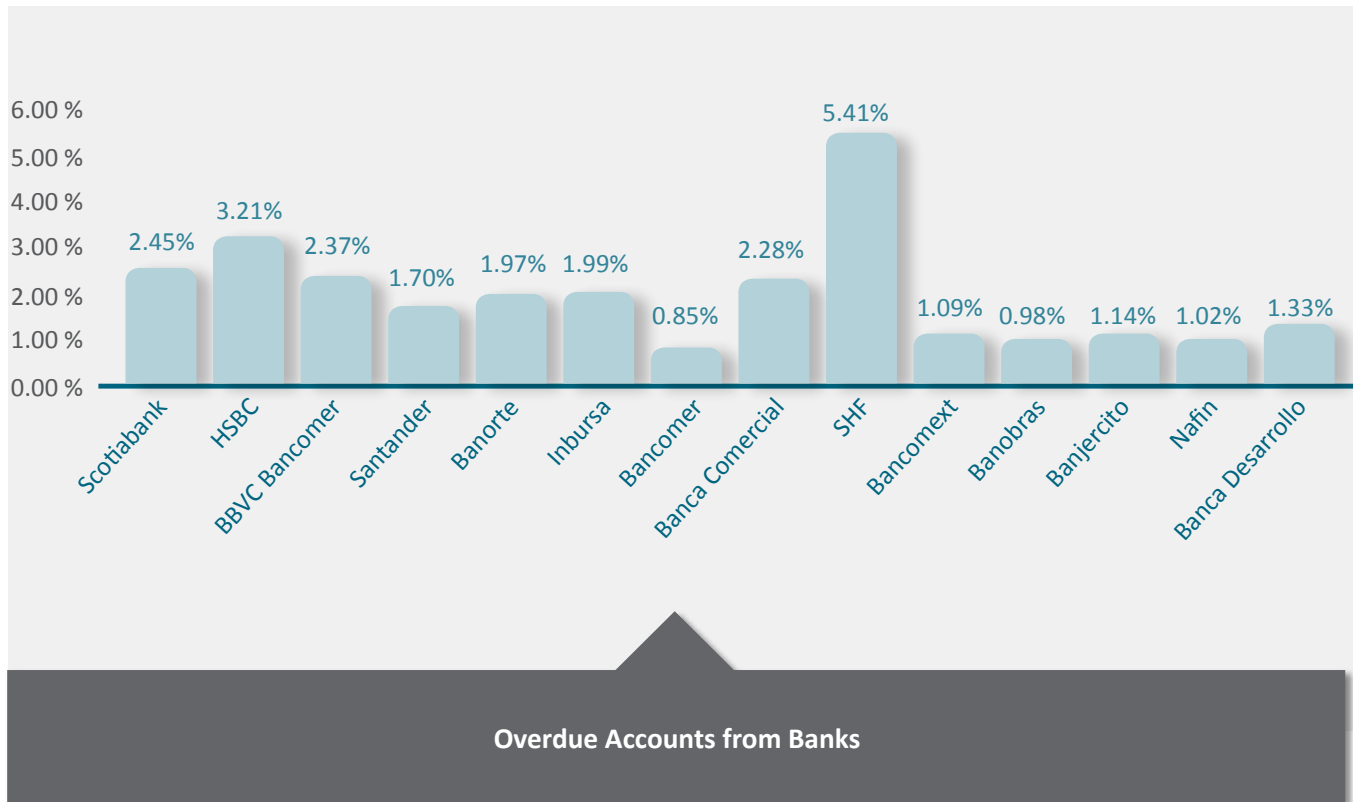
Evolution of the Overdue accounts/ Portfolio at risk

The Operative and Financial Program 2016 considers, within its main indicators, maintaining low levels, and when possible, reduce Overdue accounts/ Portfolio at risk.

At the end of December 2016, loan portfolio recorded in the balance sheet stood at 214,220 billion pesos. Overdue accounts/ Portfolio at risk, at the end of 2016, was at 2.178 billion pesos, primarily in the Financial Intermediaries Mod. "B" with 1,560 billion pesos (71.6%), Programs with 603 million pesos (27.7%) and former employees with 15.4 million pesos (0.70%).

Comparison with Other Banks

Overdue Accounts Index (OPI) of 1.02% in December 2016 places Nafin just below other development banks, excluding Federal Mortgage Society (Sociedad Hipotecaria Federal, or SHF), which has an OPI of 5.41%.



Also, Nafin compares favorably with the 2.28% of commercial banks (Banca Comercial) as of December 2016, as well as with the main commercial banks: Inbursa, Banorte, Santander, BBVA Bancomer, HSBC and Scotiabank, except Banamex.

Program portfolios, Banks and Mode "A", IF Public Sector and Decentralized Entities that make up 47.06% of the total portfolio at risk, remain with no Overdue Accounts.

Except trusts that support the development of housing and commercial banks (first-tier) credit which was recorded in June 2016, nonperforming Overdue Accounts have been contained. This considering continuity planning strategies implemented, among which are:

- Issuance of early alerts, derived from the supervision visits and follow-up of the first and second tier portfolio, which favor the timely decision-making.
- Direct payment collection, through visits programs to the borrowers' homes that have a higher recovery risk, negotiating payment proposals or loan restructuring, with the previous authorization of authorized bodies.
- Strategies of preventive reserves and loan penalty application, authorized by the Board of Directors.
- More control and follow-up in Overdue Accounts administration through the Recovery and Follow-up System, which has allowed a close approach, negotiation and follow-up of portfolio with Overdue Accounts relevant for both intermediaries and first tier companies.
- Training to staff responsible for oversight functions, monitoring and recovery of credit and guarantees portfolio, in order to increase their knowledge and skills directly related thereto (staff competencies).



Thus, Nafin has a team of executives specializing in supervision of first and second-tier loans and projects, as well as selective and securities guarantees and collections, and this has enabled to limit and reduce delinquency rates, through both prevention and correction.

Balance Sheet

As of December 2016, Nafin assets had reached a total of 515.075 billion pesos, financed with liabilities in the amount of 488.365 billion pesos which, in turn, consist of 202.689 billion pesos from repo creditors, 213.222 billion pesos corresponding to internal debt, and 72.453 billion pesos corresponding to external debt and other liabilities.

In addition, Nafin has a Financial Agent capital of 364.371 billion pesos, an amount representing a growth of 72.488 billion pesos during the year, equivalent to 24.8%. Capital for stand-by guarantees reached a level of 63.536 billion pesos, with a 6.7% growth rate when compared to the previous year, due to the dynamism and acceptance of Nafin's guarantees program.

An analysis of Nafin's financial statements for the 2016 period is provided in this report's Annex B, "Report on Consolidated Financial Statements with Subsidiaries, as of December 31, 2016."



INTERNAL CONTROL

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During 2016, the Internal Control Body (OIC) carried out its activities in accordance with an Operative Risk Management Model aligned with strategic planning by Nafin and SFP, covering the compliance with stipulations by regulatory entities; identification of critical processes and relevant information. In this context, the main lines of action focused on five areas:

1. **Modernization of Management.** Aimed at promoting a continued modernization, by standardizing processes, regulatory improvement, orientation of structure towards strategic objectives, professionalization of human resources and the use of information and communications technologies.
2. **Application of Resources.** Oriented to efficient use of financial and material resources, as well as the promotion of public hiring schemes, preferably electronically.
3. **Accountability.** Focused on increasing transparency, citizen participation, improve file management, access to information and open data generation.
4. **Legality.** Involves OIC activity regarding responsibilities, complaints, investigations, reconciliations and penalties to bidders, suppliers and contractors.

5. **Monitoring, Evaluation and Audit.** Considers OIC action around the internal control system, government assessment and public audit.

The main actions taken by OICs are focused on:

- Auditing and monitoring the implementation of preventive and corrective measures.
- Verifying compliance with the action lines of Program for a PGCM applicable to Nafin, through monitoring and support in advancing the commitments and indicators of the program.
- Diagnostics to promote process improvement and efficiency in the use of IT tools.
- Contribute through participation in the Committee on Ethics and Prevention of Conflicts of Interest in: the annual updating of the Code of Conduct; definition of a complaint procedure; development of a protocol for receiving, analyzing and dealing with complaints, and; preparation of the Committee's operation manual. It also provided support to the process for the nomination or appointment of directors in the event of sexual harassment and participating in the analysis of accusations presented to the Committee.



- To continue the communication campaign on the importance of proper use of government procurement tool called CompraNet, as well as conducting regular actions to strengthen the quality of information contained in this tool.
- Knowing citizen satisfaction with the service called “Formación empresarial presencial” (or face-to-face business training) by applying in person surveys, having obtained a score of 9 points.
- In coordination with Human Resources and Quality, implement actions to promote timely compliance with the filing of the Statement of Financial Position, which allowed achieve 100% compliance in the statement of amendment, and with respect to the initial and conclusion statement, it was reduced by 50% the level of failure.
- Monitor and support Nafin to promote compliance with the objectives of the National Program for Equal Opportunity and Non-Discrimination against Women.
- Provide care to 116 requests for access to information received, which were met in full within the established legal deadlines. It also participated in 40 meetings of the Transparency Committee.

The background of the top half of the page is a complex, abstract digital composition. It features a dark blue and purple color palette with glowing, semi-transparent numbers (0-9) scattered throughout. These numbers are overlaid on a network of thin white lines and dots, suggesting a data or neural network structure. In the center, there are several 3D, isometric geometric shapes, primarily cubes and rectangular prisms, rendered in shades of purple and pink. The overall effect is one of high-tech, data-driven aesthetics.

EXHIBIT

NACIONAL FINANCIERA
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Nafin Relevant Figures



Table 1

NACIONAL FINANCIERA, S.N.C., RELEVANT FIGURES			
Millions of MXN to End of Year			
Concept	2014	2015	2016
Total Assets 1/	389,750	384,828	503,541
Financing Agent Portfolio	1,013	109	94
Commercial Banks (First-tier) Portfolio	32,926	43,730	66,299
Second-tier Banks Portfolio	116,360	127,863	147,920
Total Credit Portfolio	150,299	171,702	214,313
Equity Investment in Companies	5,740	6,514	8,010
Equity Investment in Real Estate Companies	1,496	1,532	1,539
Equity Investment in Stocks	23	95	59
Internal Debt	156,019	184,342	213,222
External Debt	31,327	44,054	63,533
Previous Reserves for credit risks	3,665	3,999	4,464
Total Liabilities	376,342	371,062	488,365
Stockholders' Equity	22,942	24,096	26,710
Assets in a Trust or Agency	1,325,455	1,403,376	1,544,545
Debtor by Guarantee and Other Contingent Liability	56,359	64,414	53,520
Net Profit (Loss)	1,648	1,254	1,321
Compounding Level	15	14	13

1/ Consolidated with Subsidiaries



Table 2

OPERATION FOR PROMOTION OF PRIVATE SECTOR BY SECOND FLOOR, FIRST FLOOR AND GUARANTEES REGIONAL CLASSIFICATION Millions in MXN- Number of Companies						
Credit and Collateral Jan-Dec 2015			Credit and Collateral January-December		Percentage Variation 2015/2014	
Amount	Emp*		Amount	Emp*	Amount	Emp*
591,533	534,270	TOTAL	550,789	715,741	(6.9)	34.0
28,704	29,736	NORTH WEST	29,388	42,990	2.4	44.6
8,595	8,026	B. California Norte	9,139	17,393	6.3	116.7
2,471	2,243	B. California Sur	1,783	5,946	(27.9)	165.1
9,901	6,590	Sinaloa	10,721	6,430	8.3	(2.4)
7,738	12,877	Sonora	7,745	13,221	0.1	2.7
131,821	67,042	NORTHEAST	105,964	108,201	(19.6)	61.4
17,087	14,029	Coahuila	14,531	17,785	(15.0)	26.8
11,952	7,581	Chihuahua	11,056	8,376	(7.5)	10.5
3,821	5,367	Durango	3,925	13,421	2.7	150.1
87,760	25,010	Nuevo León	66,599	39,223	(24.1)	56.8
11,201	15,055	Tamaulipas	9,853	29,396	(12.0)	95.3
97,586	99,989	CENTER WEST	89,181	126,723	(8.6)	26.7
5,561	4,255	Aguascalientes	4,831	6,313	(13.1)	48.4
3,959	3,132	Colima	5,241	3,462	32.4	10.5
18,380	16,000	Guanajuato	14,794	18,007	(19.5)	12.5
44,239	26,493	Jalisco	41,261	27,987	(6.7)	5.6
10,635	20,161	Michoacán	8,729	30,186	(17.9)	49.7
2,484	3,856	Nayarit	1,852	5,133	(25.5)	33.1
8,340	21,522	San Luis Potosí	9,378	29,403	12.4	36.6
3,987	4,570	Zacatecas	3,094	6,232	(22.4)	36.4
285,526	218,382	CENTER	280,679	290,908	(1.7)	33.2
181,009	63,126	D.F.	183,261	88,029	1.2	39.4
3,155	14,167	Guerrero	2,946	32,596	(6.6)	130.1
8,187	14,149	Hidalgo	6,614	14,064	(19.2)	(0.6)
59,198	71,797	México	52,322	77,039	(11.6)	7.3
4,682	12,598	Morelos	7,430	19,518	58.7	54.9
8,875	6,342	Querétaro	8,720	9,220	(1.7)	45.4
18,729	30,591	Puebla	17,894	43,764	(4.5)	43.1
1,691	5,612	Tlaxcala	1,492	6,678	(11.8)	19.0
47,895	119,121	SOUTH-SOUTHEAST	45,577	146,919	(4.8)	23.3
6,096	7,101	Campeche	5,242	10,078	(14.0)	41.9
6,116	20,976	Chiapas	4,516	16,697	(26.2)	(20.4)
4,694	13,698	Oaxaca	3,053	15,960	(34.9)	16.5
3,353	11,171	Quintana Roo	3,594	11,745	7.2	5.1
5,225	9,719	Tabasco	5,740	13,877	9.9	42.8
16,297	44,615	Veracruz	17,329	64,168	6.3	43.8
6,114	11,841	Yucatán	6,103	14,394	(0.2)	21.6

*Emp: By Millions of People



Table 3

DEPOSITS IN MEXICAN PESOS* (MILLIONS OF MXN)			
Instrument	2014	2015	2016
Stock Exchange Certificates	28,425	40,000	50,524
PG's Nafin	111,837	87,587	108,970
New Instruments	140,262	127,587	159,494
Term Deposits in Mexican Pesos	7,153	41,153	7,153
Several Deposits	521	8	1,129
TOTAL	147,935	168,747	167,775

*Interests not included



Table 4

TOTAL EXTERNAL DEBT BALANCE AS OF DECEMBER 31ST (MILLIONS OF US DOLLARS)			
Concept	2014	2015	2016
I. Direct Debt	2,123.9	2,550.2	3,076.3
A. Deposit Certificates (London)	1,258.6	1,139.5	1,387.4
Deposit Certificates (London)	1,258.6	1,139.5	1,387.4
B. Green Bonds	-	500.0	500.0
C. Multilateral Organizations	68.2	6.3	4.5
D. Private Banking, Eximbank's and Suppliers	797.1	904.4	1,184.4
Accrued Interest	1.2	3.8	4.9
Total	2,125.1	2,554.0	3,081.2

The background of the top half of the page is a complex, abstract digital landscape. It features a dark blue and purple color palette with glowing, ethereal light trails and a grid of small, interconnected nodes. Scattered throughout are various numbers (0-9) in different colors and sizes, some appearing as 3D cubes or floating in the space. The overall effect is one of high-tech data and connectivity.

EXHIBIT

NACIONAL FINANCIERA
ANNUAL REPORT 2016

Report on Consolidated Financial
Statements with Subsidiaries,
as of December 31, 2016





**NACIONAL FINANCIERA, S. N. C.,
Development Banking Institution and Subsidiaries**

**INDEPENDENT AUDITORS' REPORT
AND CONSOLIDATED FINANCIAL STATEMENTS
AT DECEMBER 31, 2016 AND 2015**

**NACIONAL FINANCIERA, S. N. C.,
Development Banking Institution and Subsidiaries**

**INDEPENDENT AUDITORS' REPORT
AND CONSOLIDATED FINANCIAL STATEMENTS
AT DECEMBER 31, 2016 AND 2015**

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1. Independent auditors' report
- Financial statements and their notes
2. Consolidated balance sheets
3. Consolidated statements of income
4. Consolidated statements of changes in stockholders' equity
5. Consolidated statements of cash flows
6. Notes to the consolidated financial statements



Gossler, S.C.
Member Crowe Horwath International

Oficina México - Polanco
Av. Miguel de Cervantes Saavedra
No. 193 Piso 7-702
Col. Granada
11520, Miguel Hidaigo, México, D.F.
+52 (55) 2624 2111 Tel
+52 (55) 5343 7290 Fax
www.crowehorwath.com.mx

1. INDEPENDENT AUDITORS' REPORT

To the National Banking and Securities Commission

To the Ministry of Public Function

**To the Board of Directors of
Nacional Financiera, S.N.C., Development Banking Institution**

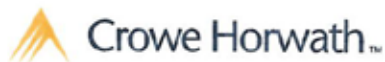
Opinion

We have audited the consolidated financial statements of **Nacional Financiera, S.N.C., Development Banking Institution and Subsidiaries** (the Institution), which comprise the consolidated balance sheets at December 31, 2016 and 2015, and the consolidated statements of income, changes in stockholders' equity, and cash flows for the years then ended, and a summary of the significant accounting policies.

In our opinion, the consolidated financial statements of the Institution at December 31, 2016 and 2015, have been prepared, in all material respects, in conformity with the General Provisions applicable to Lending Institutions, issued by the Mexican National Banking and Securities Commission (the Commission).

Basis for the opinion

We have conducted our audits in accordance with International Standards on Auditing (ISA). Our responsibilities under these standards are described below in the section Responsibilities of the auditor in relation to the audit of the consolidated financial statements of our report. We are independent of the Institution in accordance with the Code of Professional Ethics of the Mexican Institute of Public Accountants, AC (Code of Professional Ethics), along with the ethical requirements that are applicable to our audits of the financial statements in Mexico, as well as the independence requirements that external auditors must meet in accordance with the provisions of the Commission, and we have complied with the other ethical responsibilities in accordance with those requirements and with the Code of Professional Ethics. We believe that the audit evidence we have obtained provides a sufficient and adequate basis for our opinion.



Emphasis paragraph

Note 24 to the consolidated financial statements sets forth that the Institution made payments in the amounts of \$800 million and \$700 million Mexican pesos on December 9, 2016 and 2015, respectively, in accordance with the provisions in official letters numbers 102-8-023 and 102-8-077, dated December 8, 2016 and 2015, respectively, issued by the Vice Ministry of Finance and Public Credit, whereby the Federal Government instructs the Institution to make a payment under the juridical nature of benefit for furnishing a sovereign guarantee of the Federal Government. Those benefits were paid with a charge to the Institution's income and are shown in the "Other operating income (expenses)" in the consolidated statements of income of 2016 and 2015. Our opinion contains no qualifications in relation to this issue.

Key audit issues

Key audit issues are matters that, according to our professional judgment, have been of the greatest significance in our audit of the consolidated financial statements of the current period. These issues have been addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion on them, and we do not express a separate opinion on these issues. We have determined that the issues described below are key audit issues that must be disclosed in our report:

Investments in securities - Recognition and measurement

Investments in securities of the Institution were significant, since they represented 48% of total assets at December 31, 2016, whose risks were represented in the compliance with the controls that normatively guarantee their recorded entry, valuation, presentation, and confirmation of those investments.

We evaluate and test the controls that allow for assuring proper normative compliance with the recognition of investments in security at the time of their acquisition, by verifying that fair value has been measured appropriately, based on the market values furnished by a price vendor, as well as the recognition of accrued interest and its correct presentation in assets, as well as in capital gains. In addition, we obtained satisfactory confirmation of the investments that were selected to verify their existence, considering their appropriate disclosure by the Institution as well. The results of our audit tests were satisfactory.

Loan portfolio (Net) - Recognition and measurement

Considering that the substantive activity of the Institution is to grant credits, as well as the significance of the Loan Portfolio (net), which represented 41% of the total assets at fiscal year ended December 31, 2016, we identify the existence of risks as those credits are granted, including the completeness, authenticity, and valuation, jointly with the corresponding guarantees of those credits, as well as the correct calculation and determination of interest earned.

We evaluated the controls established by the Institution, both prior and subsequent to granting the credits, which were tested during our review to assure us of the proper normative compliance as of the date of the disposal of the funds, as well as the recognition of accrued interest, in conformity with the payment scheme agreed upon in the different modalities of credits. We further verified their authenticity and correct valuation of the different credits granted by the Institution, and simultaneously identified the guarantees that support the recovery thereof. In addition, we tested the correct application of the loan portfolio rating methodologies, based on the type of credits, including the analysis of the impaired portfolio. The results of our audit tests were satisfactory.

Traditional deposits - Recognition and measurement

Traditional deposits of the Institution at December 31, 2016, which represents 49% of the total liabilities, implies a material risk in the controls that refer to the timeliness of their recognition and subsequent valuation, jointly with the correct determination of interest derived from that deposit, which includes the issue of stock exchange certificates, both in the country and abroad.

Our audit procedures included, among other things, evaluating and testing the recognition policies of liabilities due to the deposit of funds, through deposit certificates, fixed term deposits, loans from domestic and foreign banks, as well as bank bonds, verifying that their entry recorded is based on the contractual value of the obligation, and that accrued interest has been recognized in income for the year. In addition, we carried out valuation tests and presentation of the distinct items that comprise traditional deposits at fiscal year-end. The results of our audit tests were satisfactory.

Payables under repurchase agreements - Recognition and measurement

Payables under repurchase agreements, which represented 43% of the total liabilities of the Institution at December 31, 2016, represented a significant risk with respect to the recognition and valuation at fair value thereof, due to the obligations derived mainly from government securities, which must comply with the controls and recording policies established by the Institution.

We evaluated and tested the controls established by the Institution relative to the recognition of repurchase transactions, by considering the date contracted. We further verified their correct valuation at fair value, as well as the determination and recognition of accrued interest, in accordance with the interest method of those repurchase transactions, with the corresponding allocation to income for the year. In addition, we verified the correct normative compliance with the recognition and measurement by the Institution acts as the buyer and as seller. The results of our audit tests were satisfactory.

Contingent liabilities - Recognition and measurement

At December 31, 2016, contingent liabilities for guarantees granted by the Institution represented 82% of the total of those liabilities, whose risk was represented in the accounting recognition, jointly

with their correct presentation and disclosure by the Institution. In addition, the net revenues obtained by credit guarantees were significant, which represented 64% of the net income of the Institution, whose risk was represented in the proper compliance with the operating rules of the Guarantee Program, whereby the Institution shares the credit risk on the financing that financial intermediaries grant to them.

Our audit procedures were designed to verify that the controls established by the Institution for the accounting recognition of contingent liabilities were complied with properly, verifying their appropriate presentation and disclosure in the financial statements of the Institution. In addition, we verified the proper compliance with the operating rules relative to the Guarantee Program of the Institution. We also verified that the accounting recognition of the net revenues obtained by credit guarantees adhere to the provisions of those rules, as well as the accounting policies established by the Institution. Moreover, we verified their appropriate presentation and disclosure in consolidated net income. The results of our audit tests were satisfactory.

Responsibilities of the Management and those responsible for the Institution's governance in relation to the consolidated financial statements

Management is responsible for the preparation and fair presentation of these accompanying consolidated financial statements, in accordance with the accounting criteria applicable to lending Institutions issued by the Commission, and for the internal control that Management deemed necessary to enable the preparation of consolidated financial statements free of material deviation, due to fraud or error.

In preparing the consolidated financial statements, Management is responsible for evaluating the Institution's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless Management either intends to liquidate the Institution or to cease operations, or has no other realistic alternative.

Those responsible for the Institution's government are responsible for overseeing the Institution's financial reporting process.

Responsibilities of the auditor in relation to the audit of the consolidated financial statements.

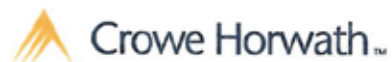
Our objectives are to obtain reasonable assurance that the consolidated financial statements as a whole are free from material misstatement, due to fraud or error, and issue an audit report that contains our opinion. Reasonable safety is a high level of safety, but it does not guarantee that an audit performed in accordance with ISAs will always detect a material deviation when it exists. Deviations may be due to fraud or error and are considered material if, individually or jointly, they can reasonably be expected to influence the economic decisions that users make based on the consolidated financial statements.

As part of an audit in accordance with ISAs, we apply our professional judgment and we maintain an attitude of professional skepticism throughout the audit. As well:

- We identify and assess the material deviation risks in the consolidated financial statements due to fraud or error, design and apply audit procedures to respond to those risks and obtain sufficient and adequate audit evidence to provide a basis for our opinion. The risk of not detecting a material deviation due to fraud is higher than in the case of a material misstatement due to error, since fraud may involve collusion, falsification, deliberate omissions, intentionally erroneous manifestations or circumvention of internal control.
- We obtain knowledge of the internal control relevant to the audit in order to design audit procedures that are appropriate to the circumstances and not for the purpose of expressing an opinion on the effectiveness of the Institution's internal control.
- We evaluate the adequacy of the accounting policies applied and the reasonableness of the accounting estimates and the corresponding information disclosed by the Management.
- We conclude on the appropriateness of Management's use of the operating accounting standard and, with the audit evidence obtained, we conclude on whether or not there is a material deviation related to facts or conditions that may generate significant doubts on the Institution's ability to continue as a functioning company. If we conclude that material uncertainty exists, it is required that we draw attention in our audit report to the corresponding information disclosed in the consolidated financial statements or, if those disclosures are not adequate, express a modified opinion. Our findings are based on audit evidence obtained to date from our audit report. Nevertheless, facts or future conditions may cause the Institution to cease to be a functioning Institution.
- We evaluate the overall presentation, structure and content of the consolidated financial statements, including disclosed information, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves reasonable presentation, in conformity with the provisions issued by the Commission.
- We obtain sufficient and appropriate evidence in connection with the financial information of the entities or business activities in the group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision, and performance of the audit of the group. We remain solely responsible for our audit opinion.

We communicate to the persons in charge of the Institution's governance, among other things, the scope and timing of the audit and the significant findings of the audit, as well as any significant deficiencies in the internal control that we identify in the course of the audit.

We also provide those responsible of the Institution's governance with a statement that we have met the applicable ethics requirements regarding independence and communicated with them about all relationships and other matters that can reasonably be expected to affect our Independence and, where appropriate, the corresponding safeguards.



Among the issues that have been the subject of communication with those responsible for the Institution's governance, we determine those that have been most significant in the audit of the consolidated financial statements of the current period and which are therefore, the key audit issues. We describe those issues in our audit report unless legal or regulatory provisions prohibit public disclosure of the matter or, in extremely rare circumstances, we determine that an issue should not be reported in our report because it can reasonably be expected that the adverse consequences thereof would exceed the benefits of public interest.

Gossler, S. C.

A handwritten signature in black ink, appearing to read "Alejandro Torres Hernández", written over a horizontal line.

Alejandro Torres Hernández
Certified Public Accountant

México City
February 15, 2017

NACIONAL FINANCIERA, S. N. C.,
Development Banking Institution and Subsidiaries
 Av. Insurgentes Sur 1971, Col. Guadalupe Inn, C.P. 01020, Mexico City

CONSOLIDATED BALANCE SHEETS
AT DECEMBER 31, 2016 AND 2015
 (Amounts in millions of pesos)
 (Notes 1 to 3)

	2016	2015		2016	2015
ASSETS			LIABILITIES		
Liquid assets (Note 5)	\$ 15,698	\$ 20,520	Traditional deposits:		
Margin accounts	-	20	Term deposits (Note 16)	\$ 143,470	\$ 125,734
Investments in securities (Note 6)			Money market		
Trading securities	220,261	161,298	Negotiable instruments issued:		
Available-for-sale securities	6,888	5,141	In the country (Note 17)		
Held-to-maturity securities	12,871	12,924	Stock certificates	51,367	40,530
	240,020	179,363	Abroad (Note 18)		
Receivables under repurchase agreements (Note 7)	20	313	Bank bonds	28,622	19,650
Derivatives (Note 8)			Securities Notes	10,352	8,655
Trading purposes	162	178		233,811	194,579
Valuation adjustment on hedges of financial assets (Note 6)	71	1,314	Interbank loans and loans for other agencies (Note 19)		
Performing loan portfolio:			Demand deposits	5,700	-
Commercial credits:			Short-term	13,339	14,030
Business or commercial activity	59,862	38,857	Long-term	11,311	9,719
Financial entities	134,329	119,788		30,350	23,749
Government entities	17,668	10,901	Payables under repurchase agreements (Note 7)	202,669	135,792
	211,859	169,546	Derivatives (Note 8)		
Consumer lending	8	7	Trading purposes	51	-
Mortgage loans	134	140	Designated as hedges	9,504	2,323
Federal government financial agent	94	109		9,555	2,323
Total performing loan portfolio	212,135	169,808	Valuation adjustment on hedges of financial liabilities (Note 8)	(3,699)	1,108
Nonperforming loan portfolio:			Other payables (Note 20)		
Commercial credits:			Taxes on earnings payable	336	364
Business or commercial activity	602	6	Employee profit sharing payable	271	257
Financial entities	1,560	1,870	Payables on liquidation of trades	88	410
	2,162	1,876	Payables for cash collateral received	1,126	5
Consumer lending	4	4	Accrued liabilities and other payables	865	667
Mortgage loans	12	14		2,686	1,723
Total nonperforming loan portfolio	2,178	1,894	Deferred credits	40	50
Loan portfolio (Note 9)	214,313	171,702	Total liabilities	475,432	359,324
Allowance for loan losses (Note 10)	(5,639)	(4,703)	STOCKHOLDERS' EQUITY (Note 23)		
Loan portfolio, net	208,674	166,999	Paid-in capital:		
Other receivables, net (Note 11)	25,807	5,142	Capital stock	8,805	8,805
Repossessed assets, net (Note 12)	9	17	Contribution for future capital increases formalized by the Board of Directors	2,750	1,950
Property, plant and equipment, net (Note 13)	1,502	1,552	Paid stock premium	8,922	8,922
Other investments (Note 14)	39	33		20,477	19,677
Permanent investments (Note 15)	9,517	7,544	Capital gains:		
Deferred taxes and PTU, net (Note 22)	775	541	Capital reserves	1,730	1,730
Other assets:			Prior year income	2,720	1,436
Deferred charges, prepaid expenses and intangibles	1,137	1,174	Gain on valuation of available-for-sale securities	(178)	(290)
Total assets	\$ 503,541	\$ 384,710	Effects of valuation in associate and affiliate companies	640	289
			Net income	1,321	1,284
				6,233	4,449
			Non-holding company equity	1,399	1,250
			Total stockholders' equity	28,109	25,356
			Total liabilities and stockholders' equity	\$ 503,541	\$ 384,710

Memorandum accounts


	2016	2015
Guarantees granted (Note 25)	\$ 72	\$ 109
Contingent assets and liabilities (Note 25)	\$ 53,448	\$ 49,738
Credit commitments (Note 25)	\$ 135,025	\$ 197,020
Assets placed in trust or mandate (Note 26)		
Trusts	\$ 1,166,459	\$ 1,108,836
Mandates	13,716	2,657
	\$ 1,180,174	\$ 1,111,493
Federal Government Financial Agent (Note 26)	\$ 364,371	\$ 291,883
Assets in custody or administration (Note 27)	\$ 593,505	\$ 552,914
Collateral received by the entity	\$ 22,298	\$ 36,602
Collateral received and sold or pledged as a guarantee by the entity	\$ 22,277	\$ 36,289
Investment bank third party trading, net	\$ 102,943	\$ 99,800
Uncollected accrued interest derived from the non-performing loan portfolio	\$ 190	\$ 297
Other memorandum accounts (Note 28)	\$ 610,807	\$ 576,917

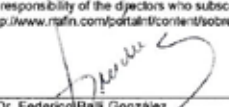
These consolidated balance sheets were prepared in conformity with the Accounting Criteria for Lending Institutions issued by the Mexican National Banking and Securities Commission, in accordance with the provisions of Articles 99, 101, and 102 of the Lending Institutions Activities Act. Those criteria, whose observance is general and mandatory, were applied on a consistent basis. The transactions carried out by the institution and reflected up to the dates referred to above were carried out and valued in accordance with sound practices and the pertinent legal and administrative provisions.


The historical balance of capital stock amounts to \$2,390.

These consolidated balance sheets were approved by the Board of Directors, under the responsibility of the directors who subscribe them.

These consolidated financial statements may be consulted on the following webpage <http://www.nafin.com/portal/contenido/sobre-nafinsa/informacion-financiera/informacion.html>


 Dr. Enrique Rogozinski Schulman
 Chief Executive Officer


 Dr. Federico Balli González
 Associate General Director of Administration and Finance


 C. P. Sergio Navarrete Reyes
 Accounting and Budget Director

The accompanying notes are part of these consolidated financial statements.

NACIONAL FINANCIERA, S. N. C.,
Development Banking Institution and Subsidiaries
 Av. Insurgentes Sur 1971, Col. Guadalupe Inn, C.P. 01020, Mexico City

CONSOLIDATED STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015
 (Amounts in millions of pesos)
 (Notes 1 to 3)

	<u>2016</u>	<u>2015</u>
Interest income (Note 24)	\$ 21,187	\$ 14,416
Interest expenses (Note 24)	(16,450)	(10,101)
Financial margin	<u>4,737</u>	<u>4,315</u>
Provision for loan losses	<u>(1,532)</u>	<u>(1,253)</u>
Financial margin adjusted by credit risks	3,205	3,062
Commission and fee income (Note 24)	2,771	2,662
Commission and fee expense (Note 24)	(289)	(298)
Loss on brokerage (Note 24)	(746)	(413)
Other operating income (expenses) (Note 24)	141	18
Administration and promotion expenses	<u>(3,181)</u>	<u>(3,298)</u>
Operating income	1,901	1,733
Equity in losses of unconsolidated subsidiaries and associates	<u>(6)</u>	<u>(11)</u>
Income before taxes on earnings	1,895	1,722
Current income taxes (Note 22)	(824)	(716)
Deferred income taxes, net (Note 22)	<u>279</u>	<u>324</u>
Net income	1,350	1,330
Non-holding company equity	<u>(29)</u>	<u>(46)</u>
Net income including controlling company equity	<u>\$ 1,321</u>	<u>\$ 1,284</u>


These consolidated statements of income were prepared in conformity with the Accounting Criteria for Lending Institutions issued by the Mexican National Banking and Securities Commission, in accordance with the provisions of Articles 99, 101, and 102 of the Lending Institutions Activities Act. Those criteria, whose observance is general and mandatory, were applied on a consistent basis. All the income and expenditures derived from the transactions carried out by the Institution and reflected during the periods referred to above were carried out and valued in accordance with sound practices and the pertinent legal and administrative provisions.

These consolidated statements of income were approved by the Board of Directors, under the responsibility of the directors who subscribe them.

These consolidated financial statements may be consulted on the following webpage <http://www.nafin.com/portalfin/content/sobre-nafinsa/informacion-financiera/informacion.html>


 Dr. Jacques Rogozinski Shtulman
 Chief Executive Officer


 Dr. Federico Balli González
 Associate General Director of Administration
 Finance


 C. P. Sergio Navarrete Reyes
 Accounting and Budget Director

The accompanying notes are part of these consolidated financial statements.

NACIONAL FINANCIERA, S. N. C.,
Development Banking Institution and Subsidiaries
 Av. Insurgentes Sur 1971, Col. Guadalupe Inn, C.P. 01020, Mexico City

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015
 (Amounts in millions of pesos)
 (Notes 1 to 3)

	Capital contributions			Capital gains				Total stockholders' equity	
	Capital stock	Capital reserves	Capital stock premium	Paid stock premium	Prior year (losses) income	Gain or loss on valuation of available-for-sale securities	Effects of valuation in associate and affiliate companies		Net income
Balances at December 31, 2014	6,805	1,950	8,922	1,730	(226)	163	1,662	1,142	24,086
Changes inherent to decisions by stockholders - Allocation of prior year income	-	-	-	-	1,682	-	(1,682)	-	-
Changes inherent to recognition of comprehensive income:	-	-	-	-	1,682	-	(1,682)	-	-
Net income	-	-	-	-	-	-	1,208	-	1,208
Gain or loss on valuation in associated and affiliated companies	-	-	-	-	-	126	-	-	126
Gain or loss on valuation of available-for-sale securities	-	-	-	-	-	(238)	-	-	(238)
Non-holding company equity	-	-	-	-	-	-	46	118	164
Changes inherent to recognition of comprehensive income	-	-	-	-	-	(238)	126	1,254	1,118
Balances at December 31, 2015	6,805	1,950	8,922	1,730	1,436	209	1,254	1,260	25,356
Restatement effect (Note 33)	-	-	-	-	-	-	30	30	30
Restated balances at December 31, 2015	6,805	1,950	8,922	1,730	1,436	280	1,284	1,260	25,386
Changes inherent to decisions by stockholders - Allocation of prior year income	-	-	-	-	1,264	-	(1,264)	-	-
Contribution for future capital increases	-	800	-	-	1,264	-	(1,264)	-	800
Changes inherent to recognition of comprehensive income - Net income	-	-	-	-	-	-	1,350	-	1,350
Gain or loss on valuation in associated and affiliated companies	-	-	-	-	-	361	-	-	361
Gain or loss on valuation of available-for-sale securities	-	-	-	-	-	112	-	-	112
Non-holding company equity	-	-	-	-	-	-	(29)	139	110
Changes inherent to recognition of comprehensive income	-	-	-	-	-	112	351	1,321	1,923
Balances at December 31, 2016	8,805	2,750	8,922	1,730	2,720	640	1,321	1,399	28,109

These consolidated statements of changes in stockholders' equity were prepared in conformity with the Accounting Criteria for Lending Institutions issued by the Mexican National Banking and Securities Commission, in accordance with the provisions of Articles 99, 101, and 102 of the Lending Institutions Activities Act. Those criteria, whose observance is general and mandatory, were applied on a consistent basis. All the movements in the stockholders' equity accounts derived from the transactions carried out by the Institution during the periods referred to above were carried out and valued in accordance with sound practices and the pertinent legal and administrative provisions.

These consolidated statements of changes in stockholders' equity will be approved by the Board of Directors, under the responsibility of the directors who subscribe them.

These consolidated financial statements may be consulted on the following webpage <http://www.nafin.com/portal/contenidos/nafin/nafininformacion-financiera/informacion.html>



Dr. Jacques Rogozinski Schtliman
 Chief-Executive Officer



Dr. Federico Balli Gonzalez
 Associate General Director of Administration and Finance



C.P. Sergio Navarrete Reyes
 Accounting and Budget Director

NACIONAL FINANCIERA, S. N. C.,
Development Banking Institution and Subsidiaries
 Av. Insurgentes Sur 1571, Col. Guadalupe Inn, C.P. 01020, Mexico City

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015
 (Amounts in millions of pesos)
 (Notes 1 to 3)

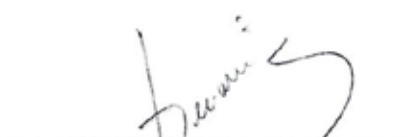
	<u>2016</u>	<u>2015</u>
Net income	\$ 1,321	\$ 1,284
Adjustments on items that do not imply cash flow:		
Allowance for uncollectible or doubtful accounts	161	208
Depreciation of property, furniture and equipment	38	35
Provisions	(131)	793
Taxes on earnings due and deferred	545	392
Equity in earnings of unconsolidated subsidiaries and associates	6	11
Others	136	(842)
	<u>755</u>	<u>597</u>
OPERATING ACTIVITIES:		
Change in margin accounts	20	(19)
Change in investments in securities	(58,755)	29,516
Change in receivables under repurchase agreements (repos)	293	4,259
Change in derivatives (asset)	7,842	50,269
Change in loan portfolio (net)	(34,079)	(16,795)
Change in repossessed assets	5	1
Change in other operating assets	(20,774)	(2,117)
Change in traditional deposits	28,759	23,173
Change in interbank loans and loans for other agencies	3,793	7,891
Change in payables under repurchase agreements	66,596	(45,692)
Change in derivatives (liability)	(2,233)	(44,316)
Change in other operating liabilities	(166)	(4,680)
Payment of taxes on earnings	(953)	(935)
Net cash flows from operating activities	<u>(9,652)</u>	<u>555</u>
INVESTING ACTIVITIES:		
Collection of disposition of property, furniture and equipment	13	-
Payment on acquisition of property, furniture and equipment	(1)	(18)
Collections on disposition of subsidiaries and associates	114	15
Payments on acquisition of subsidiaries and associates	(1,337)	(945)
Collections of cash dividends	4	2
Net cash flows from investing activities	<u>(1,207)</u>	<u>(945)</u>
FINANCING ACTIVITIES:		
Contributions for future capital increases	800	-
Net cash flows from financing activities	<u>800</u>	<u>-</u>
Net (decrease) increase in cash and cash equivalents	(7,983)	1,490
Effects of changes in the value of cash and cash equivalents	3,161	925
Cash and cash equivalents at beginning of period	20,520	18,105
Cash and cash equivalents at end of period	<u>\$ 15,698</u>	<u>\$ 20,520</u>


These consolidated statements of cash flows were prepared in conformity with the Accounting Criteria for Lending Institutions issued by the Mexican National Banking and Securities Commission, in accordance with the provisions of Articles 99, 101, and 102 of the Lending Institutions Activities Act. Those criteria, whose observance is general and mandatory, were applied on a consistent basis. All the cash inflows and cash outflows derived from the transactions carried out by the Institution and reflected during the periods referred to above were carried out and valued in accordance with sound practices and the pertinent legal and administrative provisions.

These consolidated statements of cash flows were approved by the Board of Directors, under the responsibility of the directors who subscribe them.

These consolidated financial statements may be consulted on the following webpage <http://www.nafin.com/portafin/content/sobre-nafinsa/informacion-financiera/informacion.html>


 Dr. Jacques Rogozinski Schtulman
 Chief Executive Officer


 Dr. Federico Balli González
 Associate General Director of Administration and Finance


 C.P. Sergio Navarrete Reyes
 Accounting and Budget Director

The accompanying notes are part of these consolidated financial statements.

NACIONAL FINANCIERA, S. N. C.,
Development Banking Institution and Subsidiaries
Av. Insurgentes Sur 1971, Col. Guadalupe Inn, C.P. 01020, México City

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
AT DECEMBER 31, 2016 AND 2015
(Amounts in millions of pesos, except where indicated)

NOTE 1. INCORPORATION AND BUSINESS

Organization

Nacional Financiera, S.N.C. (the Institution) was constituted as an implementing instrument of significant socioeconomic transformations, in order to promote the securities market and foster the mobilization of the financial resources of México, pursuant to the decree issued by the Federal Government on June 30, 1934.

It is a Development Banking Institution, which operates in conformity with the legal system of its own Internal Regulations, the Lending Institutions Act, and general Provisions applicable to lending institutions (the Provisions) issued by the Mexican National Banking and Securities Commission (the Commission).

Business

Contribute to the development of companies, by providing them with access to financing products, training, technical assistance and information, in order to foster competitiveness and productive investment; promote the development of strategic sustainable projects for the country on an orderly and centered basis, under schemes that allow for correcting market failures in coordination with other development banks; further regional and sectoral development of the country, particularly in the states with less relative development, through an offer of differentiated products, in accordance with the productive vocations of each region; develop financial markets and risk capital industry in the country so that they may serve as sources of financing for enterprising business people and small and medium-sized companies; Be an efficiently managed Institution, based on a consolidated corporate government structure that assures an ongoing, transparent operation, as well as the preservation of its capital in real terms, in order for it not to represent a financial burden for the Federal Government.

Nafin's Internal Regulations:

Article 2.- Nacional Financiera, S.N.C., Government-Controlled Development Bank, Development Banking Institution shall promote savings and investment, as well as channel financial and technical supports to industrial development and, in general, to national and regional economic development of the country.

The Institution shall operate and function in accordance with the applicable legal framework and sound practices and banking uses to reach the general objectives set forth in Article 4 of the Lending Institutions Act.

Lending Institutions Act:

Article 4.- The State shall exercise the guide the Mexican Banking System, in order for this System to channel its activities fundamentally to support and promote the development of the nation's productive forces and growth of the national economy, based on a sovereign policy, which encourages savings in all sectors and regions of Mexico, and its appropriate allocation to a broad regional coverage that is conducive to the decentralization of the System itself, in accordance with sound practices and bank uses.

Development Banking Institutions shall take care of the productive activities that Congress determines as a specialty in each one of these activities in the respective internal regulations.

The Institution realizes its operations by following Development Banking financing criteria, and channeling its resources mainly through first level banking and non-banking financial intermediaries. The main sources of resources of the Institution come from loans from international development institutions such as the International Reconstruction and Development Bank (World Bank) and the Inter-American Development Bank (IDB), lines of credit from foreign banks and the placement of securities on international and domestic markets.

At December 31, 2016 and 2015, the Institution's operating structure abroad includes two branches, one in London (England) and the other in the Grand Cayman Island.

Article 10 of the Institution's Internal Rules sets forth that the Federal Government will be liable at all times for the transactions carried out by the Institution with domestic individuals or legal entities, those carried out with private, governmental or inter-governmental private institutions, and the deposits received as set forth in Articles 7 and 8 in the terms of the Law on that subject matter.

NOTE 2. BASIS OF PRESENTATION

- Consolidation of financial statements** - The consolidated financial statements include the financial statements of the Institution and those of its subsidiaries over which it has control. In addition, its shareholdings in its capital stock are shown below:

	% of equity participation shares	
	2016	2015
Financial activities:		
Operadora de Fondos Nafinsa, S.A. de C.V.	99.99	99.99
Non-financial activities:		
Corporación Mexicana de Inversiones de Capital, S.A. de C.V.	78.21	76.27
Trusts:		
Sales program of securities directly to the public	100	100

	% of equity participation shares	
	2016	2015
Trust 11480 Fund for Risk Participation	100	100
Trust 11490 Fund for Surety Bond Risk Participation	100	100
Complementary services:		
Plaza Insurgentes Sur, S.A. de C.V.	99.99	99.99
Pissa Servicios Corporativos, S.A. de C.V. (in liquidation)	99.99	99.99

Intercompany balances and transactions have been eliminated in these consolidated financial statements.

The main purpose of the subsidiaries, financial companies, non-financial companies, trusts, and complementary service companies of the Institution) are as follows:

Operadora de Fondos Nafinsa, S.A. de C.V. -

Contribute to the development of financial markets, by encouraging small and medium-sized investors to gain access to the securities market.

Corporación Mexicana de Inversiones de Capital, S.A. de C.V. -

Invest in Private Capital funds, as well as foster productive investment in México in the medium and long-term, by encouraging the institutionalization, development, and competitiveness of the small and medium-sized company (S&ME). This company was incorporated with part of the stock portfolio of some development banking institutions in August 2006.

Trust Program of Security Sales Directly to the Public -

Manage the trust funds in order to carry out the necessary acts to develop and implement the Security Sales Directly to the Public, in conformity with the Operating Rules which, if applicable, are authorized by the Technical Committee.

Trust 11480 Fund for Risk Participation -

In order to have the vehicles that allow for meeting the institutional objectives related to the access of micro, small, and medium-sized companies of the country (MI S&ME) to formal financing, the institution implemented the guaranty program, whereby it shares the credit risk with banking and non-banking financial institutions (intermediaries) determined by the Technical Committee, which those intermediaries grant to domestic companies and individuals.

The gain on this trust for the years ended December 31, 2016 and 2015 amounts to \$983 and \$847, respectively. The effect of the main revenue of this trust is reflected in the item of Commissions and fees collected in the consolidated statement of income. These gains do not contemplate operating expenses, since the Institution, in its capacity as a Trustor, renders its support with human resources, informatics, and materials, insofar as it does not have its own organizational structure.

Trust 11490 Fund for Surety Bond Risk Participation -

Share the risk of compliance with construction performance bonds and/or procurement bonds set forth in subsection III, Article 5 of the Surety Bond Law with bonding institutions of the country organized in accordance with the Federal Bonding Institutions Law and determined by the Technical Committee, which they grant to micro, small and medium-sized companies, as well as to sole proprietors that have entered into a procurement contract of goods, services and/or public works with the Federal Public Administration.

Plaza Insurgentes Sur, S.A. de C.V. -

Render comprehensive real estate services to its main stockholder (the Institution), by leasing spaces and furniture, as well as adapting offices with preventive, corrective maintenance programs to the real property infrastructure.

Pissa Servicios Corporativos, S.A. de C.V. (in liquidation) -

Render complementary and auxiliary services in managing and realizing the corporate objective of any National Lending Institution that is or eventually becomes its stockholder, as well as auxiliary companies and trusts thereof.

Comprehensive income - This is the change of stockholders equity during the year for items that are not distributions and changes in paid-in capital. It consists of net gain for the year plus other items that represent a gain of the same period, which are presented directly in stockholders equity, without affecting the statement of income.

NOTE 3. SIGNIFICANT ACCOUNTING POLICIES

The Institution's significant accounting policies concur with the accounting criteria set forth by the Commission, which are included in the Provisions, their circulars, as well as general official and particular letters that it has issued for that purpose. Those criteria require that Management realize certain estimates and use certain assumptions to determine the valuation of some items included in the consolidated financial statements, as well as to make some disclosures that are required to be presented therein. Even when they can eventually differ from their final effect, Management considers that the estimates and assumptions used were adequate under current circumstances.

These accounting criteria will be apply suppletorily when, in the absence thereof, Financial Reporting Standards (FRS) issued by the Mexican Board of Financial Reporting Standards (CINIF) are observed.

Accounting changes.

Beginning January 1, 2016, the Institution adopted the following FRS and Improvements to FRS issued by the CINIF, which became effective as of the above date. These FRS and Improvements to FRS did not have a significant application in the consolidated financial information presented by the Institution, which are discussed below:

FRS D-3 "Employee benefits" - FRS D-3 is effective for years beginning on or after January 1, 2016 with retrospective effects and early adoption is allowed as of January 1, 2015. FRS D-3 supersedes the provisions in FRS D-3.

The main changes included are as follows:

- **Direct Benefits:** the classification of direct benefits was modified in the short-term in direct benefits, and the recognition of deferred Employee Profit Sharing was ratified.
- **Termination benefits:** The bases were modified for identifying when payments for labor disconnection actually meet the postemployment benefit conditions and when they are termination benefits.
- **Postemployment benefits** – Among others, the following were modified: the accounting recognition of multi-employer plans; government plans and plans of entities under common control; the recognition of the net defined benefit liability (asset); the bases for determining the actuarial hypothesis in the discount rate; the recognition of the Service Cost of Past Periods (SCPP) and of the Early Settlement of Obligations (ESO).
- **Remeasurements:** In recognizing post-employment benefits, the corridor approach is eliminated in the treatment of the plan's profits and losses (PPL); therefore, they are recognized as accrued and recognized directly in Other Comprehensive Income ("ORI"), requiring their recycling to the period's net profit or loss under certain conditions.
- **Plan assets Ceiling (PA)** – Identifies a plan asset ceiling and specifies which entity contributed funds do not qualify as such.
- **Recognition in income of Plan Amendments (PA), Personnel Reductions (PR), and early liquidations of Obligations (LAO)** in postemployment benefits, and all CLSP are recognized immediately in income.

- Discount rate: it sets forth that the discount rate of the Defined Benefits Obligation DBO is based on high quality bond rates with a deep market and, in the absence thereof, on governmental bond rates.
- Termination benefits require that it be analyzed if payments for termination or separation qualify as termination benefits or if they are post-termination benefits. It further sets forth that if it is a non-cumulative benefit without pre-existing conditions for being granted, it is a termination benefit and, therefore, it sets forth that it must not be recognized until the event takes place. However, if there are pre-existing conditions, either by contract, law or payment practices, it is considered a cumulative benefit, and it must be recognized as a postemployment benefit.

Improvements to 2016 FRS:

The following improvements were effective beginning January 1, 2016, with The modifications that bring about accounting changes are listed below:

FRS C-1, Cash and cash equivalents, and FRS B-2, Statement of cash flows:

These are modified to consider foreign currency as cash and not as cash equivalents. Moreover, it explains that both opening and final valuation of cash equivalents must be carried out at fair value.

Bulletin C-2, Financial instruments and Amendment to Bulletin C-2:

- a) The definition of financial instruments available-for-sale is modified to clarify that they are instruments that have the intent of being traded in the medium-term from the time at which they are invested in and on dates prior to their maturity, in order to obtain gains based on their changes in their value on the market, and not only through yields inherent thereto.
- b) Criteria are defined that must be taken into account for an entity to be able to classify a financial instrument as available-for-sale, which is not possible when: i) there is an intent to hold it for an undefined period; ii) the entity is willing to sell the financial instrument; iii) there is a put option or a call option in favor of the instrument; and iv) the issuer of the instrument is entitled to liquidate the financial instrument at a significantly lower amount than its redeemed cost.
- c) The concept of purchase expenses is eliminated and the definition of transaction costs is incorporated.
- d) Impairment losses are permitted to be reversed related to held-to-maturity financial instruments in net income or loss for the period.

Bulletin C-10, Derivative financial instruments and hedging transactions:

This Bulletin sets forth that at the inception of the hedge in the periods subsequent to and at the date of the financial statements, hedge effectiveness must be evaluated and the method used to measure effectiveness must be defined as well.

- a) It explains how to designate a primary position.
- b) Accounting recognitions of the transaction costs of a derivative financial instrument is modified to be recognized directly in the net income or loss for the period at the time of acquisition and not be amortized over its period of effectiveness.
- c) Specifies about the recognition of embedded derivative financial instruments.

The significant accounting criteria followed by the Institution are summarized below:

1. **Recognition of the impact of inflation on the financial information** - Accumulated inflation of the last three prior annual fiscal years at December 31, 2016 and 2015 is 9.65% and 10.06%, respectively; therefore, the economic environment qualifies as non-inflationary in both fiscal years. The percentages of inflation for the years ended December 31, 2016 and 2015 were 3.37% and 2.10%, respectively. The financial statements recognize the impact of inflation up to December 31, 2007.
2. **Liquid assets** - These assets are valued at their nominal valued and with respect to foreign currency, they are valued at their fair value based on the year end quote.

The currencies acquired that are agreed upon to liquidate on a date subsequent to the realization of the buy and sell transaction are recognized as a restricted asset (foreign currency receivable). Foreign currency sold is recorded as a credit to liquid assets (foreign currency deliverable). The offsetting entry is recorded in a debit clearing account when a sale is realized and a credit clearing account when a purchase is realized.

For purposes of presentation of the financial information, foreign currency clearing accounts receivable and deliverable are offset and presented in the item of other receivables (net) or other payables, as applicable.

This item also includes interbank lending transactions agreed upon in a term less than or equal to 3 business days, as well as other liquid assets such as correspondent banks, sight drafts, and coined precious metals.

3. **Margin accounts** - The so-called margin accounts (security deposits) for derivative financial instrument trading on recognized markets are recognized at nominal valor. Security deposits are intended to assure compliance with obligations corresponding to derivatives carried out on recognized markets and correspond to the opening margin and subsequent contributions or retirements realized in the duration of the respective contracts.
4. **Valuation of foreign currency** - The Institution maintains accounting records by type of foreign currency in assets and liabilities contracted in a foreign currency, which are valued at the fixed exchange rate published by the Banco de México (Banxico) in the Official Daily Gazette on the business day subsequent to the date of the transaction or preparation of the financial statements, as applicable.
5. **Investments in securities** - The record and valuation of investments in securities are subject to the following guidelines:

Trading securities:

These securities deal with the Institution's own positions acquired with the intent of selling them and obtaining gains from price differences resulting from short-term trading operations. Those securities are realized with market participants.

At the time of their acquisition, they are initially recognized at their fair value (which, if applicable, includes the discount or surcharge) and corresponds to the price agreed upon. They are subsequently valued at fair value, by applying market values furnished by an independent pricing service, authorized by the Commission. The book effect of this valuation is recorded in income for the year. Fair value of debt securities includes both the capital component and interest accrued on the securities.

On the date sold, the gain or loss is recognized on the trade for the spread between its carrying value and the sum of the considerations received.

Cash dividends collected on the net equity instruments are recognized in income for the year at the time at which the right to receive the payment thereof is generated.

Available-for-sale securities:

These are those debt securities and net equity instruments, whose intent is intended to obtain earnings derived from the price differences resulting from short-term trading operations. In the case of debt securities, there is neither any intent nor capacity to hold them to maturity; therefore, it represents a residual category, that is, they are acquired with an intent other than that of trading securities or held-to-maturity securities, respectively.

At the time they are acquired, they are initially recognized at their fair value, which corresponds to the price agreed upon. They are subsequently valued at fair value, by applying market values furnished by an independent pricing service, authorized by the Commission. The book effect of this valuation is recorded in stockholders' equity. Fair value of debt securities includes both the capital component and interest accrued on the securities.

On the date sold, the gain or loss is recognized on the trade for the spread between its carrying value and the sum of the considerations received, and the effect of accrued valuation that has been recognized in stockholders' equity.

Cash dividends collected on the net equity instruments are recognized in income for the year at the time at which the right to receive the payment thereof is generated.

Held-to-maturity securities

These are those debt securities, whose payments are fixed or determinable with a fixed maturity (which means that the contract defines the amounts and dates of the payments to the holding entity) with respect to which the Institution has both the intent and the capacity to hold up to their maturity.

They are initially recognized at their fair value at the time when they are acquired, which corresponds to the agreed upon price, and applied to income for the year on accrued interest. The gain or loss is recognized on the trade for the spread between its net realization value and its carrying value on the date sold.

The transaction costs of the acquisition of the securities will be recognized depending upon the classification in which they are designated, as follows:

- a) Trading securities. - In income for the year on the date of acquisition.
- b) Available-for-sale and held-to-maturity securities. - Initially as part of the investment.

In the event of reclassifying from the category of held-to-maturity securities to available-for-sale securities, provided that there is neither the intent nor the ability to hold them to their maturity.

Should trading securities be reclassified to available-for-sale securities, they may only be reclassified in extraordinary circumstances pursuant to express authorization of the Commission.

The gain or loss on valuation that corresponds to the reclassification in the event of reclassifying held-to-maturity securities to available-for-sale securities will be recognized in other comprehensive income items in Stockholders' Equity.

For securities that would have been authorized to be reclassified from the category of available-for-sale securities to the category of held-to-maturity securities, the gain or loss on valuation that corresponds to the transfer date should continue in Stockholders' equity, and it will be amortized based on the probable life of the reclassified securities

6. **Impairment of the value of a security** - The Institution evaluates if there are objective indicators that a security is impaired at the date of the balance sheet.

A security is considered impaired and, therefore, an impairment loss is incurred if, and only if there are objective impairment indicators as a result of one or more events that occur subsequent to the initial recognition of the security, which had an impact on its estimated future cash flows that can be determined reliably. It is not very likely to identify a single event that is individually the cause of such impairment. It is more feasible that the combined effect of various events might have caused the impairment.

7. **Repurchase transactions (repos)** - Repurchase transactions are those whereby the seller acquires the ownership of negotiable instruments for a sum of money, and is bound to transfer the ownership of other securities of the same type to the seller in the agreed upon term and against the reimbursement of the same price plus a premium. The premium is in the benefit of the seller, unless agreed upon otherwise.

Repurchase transactions are considered as a sale for legal purposes where a repurchase agreement is established of the transferred financial assets. However, the economic substance of repurchase transactions is that of financing with collateral, whereby the seller delivers cash as financing, in exchange for obtaining financial assets that serve as protection in the event of nonperformance. Repurchase transactions (repos) are recorded as indicated below:

- On the date of contracting the repurchase transaction, the Institution, acting as a seller, recognizes the cash inflow or a debit clearing account, as well as an account payable at its fair value, initially its agreed upon price, which represents the obligation to reimburse that cash to the buyer.
- Throughout the life of the repurchase transaction, the account payable is valued at its fair value, through recognition of interest on the repurchase transaction in income of the year as accrued, in accordance with the effective interest method, and making an application to that account payable.
- On the day that the repurchase transaction is contracted, when the Institution acts as the buyer it recognizes the disbursement of cash or a payable to a clearing account, as well as record an account receivable at its fair value at the price agreed upon initially, which represents the right to recover the cash delivered.

Over the life of the repurchase transaction, the receivable is valued at its fair value, through recognition of interest on the repurchase transaction in income of the year as accrued, in accordance with the effective interest method, and making an application to that account receivable.

Collateral furnished and received other than cash

Collateral furnished by the seller to the buyer (other than cash) is recognized in accordance with the following:

- a) The buyer recognizes the collateral received in memorandum accounts. The seller reclassifies the financial asset in its balance sheet, by presenting it as a restricted asset. Toward that end, the valuation, presentation, and disclosure standards are adhered to in accordance with the pertinent accounting criterion for the applicable lending institutions.
- b) Upon selling the collateral, the seller recognizes the proceeds from the sale, as well as an account payable for the obligation to return such collateral to the buyer (measured initially at the fair value of that collateral), which is valued at fair value (any spread between the price received and the fair value of the account payable will be recognized in income of the year).
- c) In the event that the seller should fail to perform the conditions set forth in the contract and, therefore, should not be able to claim the collateral, the seller should remove it from its balance sheet at its fair value against the account payable. By the same token, the buyer recognizes the receipt of collateral in its balance sheet, in accordance with the type of asset involved, against the account receivable or, if applicable, such collateral had previously been sold, the buyer writes off the account payable discussed, relative to the obligation to return such collateral to the buyer.
- d) The seller keeps the collateral in its balance sheet, and the buyer only recognizes it only in memorandum accounts, except when the risks, benefits, and control of that collateral has been transferred due to seller nonperformance.
- e) Memorandum accounts recognized for collateral received by the buyer are written off when: i) the repurchase transaction reaches maturity; ii) there is seller nonperformance; or iii) the buyer exercises the right to sell or accord and satisfaction of the collateral received.

8. *Derivative financial instruments trading and hedging transactions* - The Institution carries out two types of transactions:

- Hedging transactions when derivative financial instruments are traded in order to offset one or various financial risks generated by a transaction or set of transactions associated with a primary position.
- Trading operations when the Institution maintains a derivative financial instrument with the original intent to obtain gains based on changes in their fair value.

Hedging transactions, according profile covered exposure can be:

- a) Fair value hedge: This represents a hedge against exposure to changes in fair value of recognized assets or liabilities or unrecognized firm commitments, or of a portion identified of those assets, liabilities or unrecognized firm commitments that is attributable to a particular risk that can affect the gain or loss of the period.

This hedge should be recognized in the following manner:

- 1) The gain or loss on the valuation of the fair value hedging instrument (for a hedge derivative) or the foreign currency component valued in conformity with FRS B15 "Foreign currency translation" for a non-derivative hedging instrument) should be recognized in income for the period; and
 - 2) The gain or loss on the hedged item attributable to the hedged risk should adjust the carrying value of that item and it should be recognized in income of the period. The foregoing even applies if the hedged item is valued at cost (for example, when the interest rate risk is hedged in the loan portfolio that is valued at amortized cost). The recognition of the gain or loss on valuation attributable to the hedged risk in income for the period even applies if the hedged item is an investment in securities designated as available-for-sale.
- b) Cash flow hedge: This represents a hedge of the exposure to the change in cash flows of a forecasted transaction that: (i) is attributable to a particular risk associated with a recognized asset or liability (such as the total or some of the future interest payments applicable to a credit or debt instrument at a variable interest rate), or with a highly likely event; and that (ii) it can affect income of the period.

That hedge should be recognized in the following manner:

- 1) The portion of the gain or loss on the hedged instrument that is effective in the hedge should be recognized in stockholders' equity, and forms part of the other items of comprehensive income.
- 2) The portion of the gain or loss on the hedged instrument that is ineffective in the hedge should be recognized directly in income for the year.
- 3) Contributed capital or margin accounts managed (delivered and received) when derivative financial instruments are traded on unrecognized markets are recorded in the item of "Margin Accounts" and "Other payables and accrued liabilities", respectively.
- 4) The accounting criteria of the Commission do not consider the counterparty risk for the valuation of derivative financial instruments.

A cash flow hedge should be accounted for as follows:

- 1) The effective hedging component recognized in stockholders equity associated with the hedged item should be adjusted to equal the lower amount from between the following items:
 - i. The accumulated gain or loss of the hedging instrument since the inception thereof; and

- ii. The accumulated change in fair value (present value) of expected future cash flows of the hedged item from the inception of the hedge.
- c) A hedge of a net investment in a foreign transaction represents the portion of the gain or loss of the hedge instrument that is effective in hedging a net investment in a foreign transaction, and it should be recognized in stockholders' equity, thereby forming part of the other items of comprehensive income in the item of accumulated translation effect.

9. Foreign currency transactions - Foreign currency transactions are recorded at the current exchange rate at the date of the transaction. Foreign currency assets and liabilities are valued at the current exchange rates at the end of period exchange rates, determined and published by the Banco de Mexico.

10. Loan portfolio - Loans granted are recorded as an asset as of the date on which funds are drawn down and interest is aggregated as accrued, in accordance with the loan payment schedule.

Interest applicable to current lending operations is recognized and applied to income as accrued. Interest accrual is suspended at the time at which the unpaid balance of the loan is considered in default.

While loans remain classified as nonperforming portfolio, accrued interest is controlled in memorandum accounts. In the event that this interest should be collected, it is recognized in income of the year.

Nonperforming portfolio

The performing portfolio is transferred to the nonperforming portfolio when the unpaid balance of the current loans meets the following constraints:

- a) It is known that the borrower is declared in bankruptcy proceedings with a merchant;
- b) Loans with a single payment on principal and interest at maturity and present 30 or more calendar days in arrears;
- c) Loans with a single payment on principal at maturity and periodic payments on interest that present 90 or more calendar days in arrears of the respective interest payment or 30 or more calendar days in arrears of the principal;
- d) Loans with periodic payments on principal and interest and present 90 or more calendar days in arrears;
- e) Revolving loans that present two monthly billing periods or, if applicable, 60 or more calendar days in arrears.

- f) Monthly periods may be used with respect to terms to maturity, with the following equivalences:
- 30 days is equivalent to one month
 - 60 days to two months
 - 90 days to three months

Impaired portfolio

All those commercial credits are understood as impaired portfolio. Based on current information and events, as well as the review process of such credits, there is a considerable likelihood that both the principal component and interest of impaired portfolio may not be entirely recovered, in accordance with the terms and conditions agreed upon originally. Both the current portfolio and nonperforming portfolio may be identified as an impaired portfolio.

The significant policies and procedures for granting, controlling, and recovering loans set forth in the Institution's regulations are as follows:

- a) Loans granted or guaranteed by the Institution are for financing projects to economically and financially viable companies.
- b) The maximum limit of financing is determined based on the needs of the investment project and results of the evaluation of the creditworthiness of the company or project.
- c) The terms and periods of grace of loans are established based on the creditworthiness of companies.
- d) Collateral, preferably mortgage securities, is obtained in adequate, sufficient proportion, in accordance with the characteristics of the loans and, if applicable, in accordance with the type of financial broker that grants it.
- e) Loan securities granted by the Institution are complementary to those that must be furnished by borrowers and do not substitute those securities. Accordingly, brokers should negotiate the securities that back the loan granted with the borrowers in each case.
- f) The borrower should have proven creditworthiness and integrity.
- g) Credit granting operations of Bank Financing Brokers (IFB), as well as Non-Bank Financial Brokers (IFNB) are recorded at the offices of the parent company. Balances are reconciled with IFNB balances every month, as well as with IFB balances every quarter.
- h) Portfolio turnover is carried out through the Institutional Portfolio Recovery and Management System (SIRAC), managed at the office of the parent company by the Credit Management General Office.

- i) No new credit operations are carried out with the creditor company, as long as there are debts in arrears with that company.
- j) Out-of-court collection procedures are realized in the portfolio with nonperformance of 30 to 90 days.
- k) Once 90 days of nonperformance of a debt have elapsed, the loan balance is considered nonperforming and collection is made through legal means, either directly in the case of first tier loans or through financial brokers in the case of discounts of loans.

The Institution's main policies and procedures for the evaluation and follow-up on loans risks in accordance with the type of operation are as follows:

Second Tier Operations

- a) Modality "A" Financial Brokers defined as banks or factoring or leasing companies that form part of a financial group that includes a bank. Given the collection mechanism with a charge to its Banco de Mexico account, these brokers are considered on the lowest risk scale

A "Credit Risk Limit Assignment Methodology for Operating with Banks in México" has been established for these brokers, which sets forth the maximum credit risk levels that it is willing to accept with each one of these brokers, in both credit and discount operation, as well as financial market operations. The established limits are followed up on every day, and the limits are updated every month. Considering their high creditworthiness, supervision of the broker is carried out by monitoring the broker through the evolution of its risk rating, and annual visits are realized.

- b) Modality "B" Financial Brokers applies to all the IFNB that do not form part of a financial group that includes a bank. They are considered as a regular source of credit risk. Consequently, specific rules and regulations have been established that these brokers must comply with for brokering or trading with the Institution's resources.

Supervision mechanisms have been established for these brokers, which follow up on their financial evolution on a monthly basis, as well as compliance with the regulations that have been imposed thereon. In addition, credits granted to brokers are rated according to the drawdowns, and semester or annual supervision visits are realized based on their risk rating.

First Tier Operations

This operation is marginal for the Institution. A follow-up mechanism is established based on the portfolio credit risk rating, in accordance with the established guidelines.

Guarantee program operations

A monthly follow-up has been established for the operations portfolio of the guarantee program, which includes the analysis of harvests or crops, analysis of the results of the follow-up on the processes agreed upon with banks at a sample level, and the analysis of the financial evolution of the deeds of trust established in the Institution. Banks that participate in this program independently submit the credits supported under the guarantee program, into their credit risk follow-up policies and procedures, as well as the risk rating in accordance with the established guidelines.

- 11. Allowance for loan losses** - The Commission determines the bases for rating the loan portfolio. The provision applicable to loan risks is estimated monthly, based on quantitative and qualitative factors contemplated in the methodology for rating portfolios established by the Commission, which considers the analysis of the impaired portfolio, in accordance with the risk that it presents. NAFIN follows the practice of creating additional overall provisions to deal with possible contingencies in facing foreseeable risks.

Through the Provisions, the Commission establishes the loan portfolio rating methodologies based on the type of credits comprising it, so that it allows for:

- a) Evaluating each borrower, in the case of the consumer loan portfolio, taking into account the likelihood of nonperformance, the severity of the loss, and nonperformance exposure.
- b) Stratifying the portfolio based on the delinquency in payments which includes, in the case of the mortgage housing loan portfolio, the likelihood of nonperformance, severity of the loss, and nonperformance exposure, and the value of the credit guarantee, so that the amount of the preventive reserves required in each portfolio stratum is determined based thereon.
- c) Analyzing the creditworthiness of its debtors in the case of the commercial loan portfolio, and estimate possible losses so that the amount of the preventive reserves required is determined based thereon.
- d) Using internal methodologies prepared by the lending institutions themselves in accordance with the Provisions, when they evidence that the requirements have been met determined by the Commission for that purpose.

In accordance with the Provisions, the provision applicable to the mortgage housing and consumer loan portfolio is estimated monthly, based on the last day balances of each month.

In addition, the balances relative to the quarters that end in March, June, September, and December are used for purposes of rating the commercial portfolio. The applicable preventive reserves are recorded in the accounting at the end of every quarter, considering the balance of the debt recorded on the last day of the months referred to above. For the book entry in the two months subsequent to each quarter end, the pertinent rating is applied to the balance of the credit involved that has been used at the immediately preceding quarter, recorded on the last day of the months referred to above, when there is an interim rating subsequent to the quarter end. This rating can be applied to the balance of the debt recorded on the last day of the two months under discussion.

12. ***Other receivables, net*** - The amounts applicable to the Institution's other receivables are provided for with a charge to income for the year, regardless of the likelihood of recovery, within 60 to 90 days subsequent to their initial book entry, depending on whether or not the balances are identified, respectively.
13. ***Property, furniture and equipment net*** - Property, furniture and equipment, as well as installation expenses, and leasehold improvements are recorded at the cost of acquisition. Assets that come from acquisitions up to December 31, 2007 were restated by applying factors derived from Investment Units (UDIS) from the date of acquisition up to that date. Relative depreciation and amortization are recorded by applying a percentage to the restated cost up to that date, determined based on the estimated economic useful life thereof.
14. ***Repossessed assets or received as a dation in payment*** - These assets are recorded at the lower of the cost of adjudication or fair value reduced from the costs and expenses strictly indispensable that are disbursed in their adjudication.

Repossessed assets are valued as set forth in the Provisions, in accordance with the type of asset involved. The valuation is recorded against income for the year as other operating income (expenses).

The amount of the estimate that recognizes potential losses of value due to the elapsing of time of the repossessed assets should be determined on the adjudicated value, based on the procedures set forth in the Provisions, and recognized in income for the year as other operating income (expenses).

In the event that the estimate referred to in the prior paragraph should be modified in accordance with the Provisions referred to above, that adjustment should be recorded against the amount of the previously recognized estimate as operating income (expenses).

At the time when repossessed assets are sold, the difference between the selling price and carrying value of the repossessed asset, net of estimates, should be recognized in the income for the year as other operating income (expenses).

- 15. Taxes on earnings** - Income tax is recorded in income for the year in which it is current and payable. Deferred tax on earnings will be determined applying the applicable rate to the temporary differences that result from comparing book and tax values of assets and liabilities and, if applicable, the benefits of tax loss carryforwards and some tax credits are included. The deferred tax asset is recorded only when there is a high likelihood that it can be recovered.
- 16. Other investments and permanent investments** - These are permanent investments in trusts and stock of companies in which there is no joint control, nor significant influence. They are initially recorded at the cost of acquisition. They are valued by using the equity method, considering the financial information relative to such entities when there is a practical impossibility of obtaining financial information from entities. The investment is adjusted to a zero value or its cost of acquisition. The adjustment procedure is selected by considering the prudential application criterion of the particular rules contained in FRS.
- 17. Traditional deposits** - The liabilities for attracting funds through certificates of deposit, fixed term deposits, bank acceptances, promissory notes with liquid yield at maturity, loans from domestic and foreign banks, and bank bonds are recorded based on the contractual value of the obligation. Accrued interest is recognized in income for the year as interest expense.
- 18. Interbank loans and from other agencies** - Liabilities from interbank loans are recorded based on the contractual value of the obligation. Accrued interest is recognized directly in income of the Institution as interest expense.
- 19. Short-term direct employee benefits** - Such benefits are valued in proportion to the services rendered considering current salaries, and the liability is recognized as accrued. It mainly includes Employee Profit Sharing payable, compensated absences such as vacations, and vacation premium, and incentives.
- 20. Long-term direct employee benefits** - The payments set forth by the Federal Labor Law and General Working Conditions (GWC) in effect to employees and workers who no longer render their services are recorded as follows:

Indemnities-

Non-substitutive payments of a retirement made to personnel who retire under certain circumstances are recorded as accrued, which are calculated by independent actuaries, based on the projected unit credit method by using nominal interest rates.

Seniority premium-

Seniority premiums payable to employees that have completed fifteen or more years of service, as provided for in the Federal Labor Law, are recognized as a cost during the years of service of personnel. Toward that end, there is a provision that covers the defined benefit obligation, which is calculated by actuarial calculations based on the projected unit credit method by using nominal interest rates.

In accordance with the Federal Labor Law, the Institution has a liability for indemnifying employees who are dismissed under certain circumstances, and an obligation to pay a seniority premium when they retire voluntarily (provided that they have completed fifteen or more years of service). They are dismissed for a justified reason and those who are terminated, regardless of whether or not for a justified cause, in the event of disability or they are invalid and, in case of the worker's death.

- 21. Provisions** - Provisions are recognized when the Institution has a present obligation derived from a past event that probably results in the disbursement of economic resources (funds) and can be reasonably estimated.
- 22. Employee Statutory Profit Sharing (ESPS)** - ESPS is recorded in income for the year in which it becomes due, and it is presented in the item of other income and expenses in the accompanying statement of income. Deferred employee profit sharing is determined by temporary differences resulting from comparing book and tax values of assets and liabilities. It is only recognized when it is likely that a liability will be liquidated or a benefit will be generated and there is no indicator that this situation is going to change, in such a way that this liability or benefit does not materialize.

Employee Profit Sharing is determined based on taxable income, in accordance with Article 9 of the Income Tax law (ISR Law). At December 31, 2016 and 2015, Employee Profit Sharing amounted to \$271 and \$257, respectively.

- 23. Recognition of interest** - Interest generated on lending operations in effect are recognized and applied to income based on the accrued amount. Interest applicable to the nonperforming portfolio is applied to income at the time it is collected. Yields on interest relative to investments in securities are applied to income based on what is accrued.

Interest relative to borrowing operations re recognized in income as accrued, regardless of their due date.

For purposes of presentation of the statement of income, fees, premiums, and foreign exchange transactions are included in the item of interest income.

Fees charged for the initial granting of credits are recorded as a deferred credit, which is amortized as interest income, under the straight-line method during the life of the credit.

- 24. Brokerage fees** - Given the role of involvement realized by the Institution as a means of liaison between the lender of financing and the borrower, the Institution obtains a fee for its work of negotiating credits on the markets. That fee is recorded in the statement of income when generated in the item of "Commission and fee income".
- 25. Gain or loss on brokerage** - Gains or losses on brokerage derived from securities and derivative instruments trading, valuations at fair value of investments in securities and derivative financial instruments, and the recognition of the increase or decrease in the value of investments in securities.
- 26. Trusts** - The operations in which the Institution acts as a Trustee are recorded and controlled in memorandum accounts. In accordance with the ISR Law, the Institution acting as a Trustee is responsible for compliance with the tax obligations of the trusts that realize business activities up to the amount of the trust assets.
- 27. Foreign currency transactions** - Monetary assets and liabilities, as well as the items of the statements of income of foreign subsidiaries are translated at the closing exchange rate of the valuation date.
- 28. Clearing accounts** - For purposes of presentation of the financial statements, the balance of debit and credit clearing accounts may be offset, provided that they are derived from the same type of transactions, which have been carried out with the same counterparty and are liquidated on the same maturity date.
- 29. Impairment of long-lived assets** - The Institution reviews the carrying value of the long-lived assets in use with respect to the presence of any impairment indicator that might indicate that the carrying value might not be recoverable, considering the higher present value of the future net cash flows or the net selling price in the event of their eventual disposition. The impairment is recorded if the carrying value exceeds the higher of the values discussed above.

At December 31, 2016 and 2015, the Institution's long-lived assets do not present any impairment indicators.

NOTE 4. FOREIGN CURRENCY POSITION

At December 31, 2016 and 2015, the foreign currency position valued in local currency is summarized as follows:

	<u>2016</u>	<u>2015</u>
Assets	\$ 127,575	\$ 66,460
Liabilities	(127,620)	(67,226)
(Short) long position	<u>\$ (45)</u>	<u>\$ (766)</u>

At those same dates, foreign currency assets and liabilities (millions) are as follows:

	<u>2016</u>			<u>2015</u>
	<u>Assets</u>	<u>Liabilities</u>	<u>Net</u>	<u>Net</u>
US dollars	6,157	6,163	(6)	(48)
Japanese yen	1	-	1	5
Euros	25	24	1	1
Pounds sterling	2	-	2	2
Special draft fee	1	1	-	-

Those foreign currency assets and liabilities are valued and documented in local currency as follows:

	<u>2016</u>			<u>2015</u>
	<u>Assets</u>	<u>Liabilities</u>	<u>Net</u>	<u>Net</u>
US dollars	\$ 126,947	\$ 127,057	\$ (110)	\$ (826)
Japanese yen	-	-	-	1
Euros	544	529	15	8
Pounds sterling	57	7	50	51
Special draft fees	27	27	-	-
	<u>\$ 127,575</u>	<u>\$ 127,620</u>	<u>\$ (45)</u>	<u>\$ (766)</u>

At December 31, 2016 and 2015, the value of the US dollar is equivalent to 20.6194 and 17.2487 Mexican pesos per US dollar, in conformity with the exchange rate published by Banxico, respectively. Other currencies are valued considering their exchange rate in connection with the US dollar.

At the date of this report, the value of the US dollar is equivalent to 20.3254 mexican pesos per US dollar, in conformity with the exchange rate published by Banxico. Other currencies are valued considering their exchange rate in connection with the US dollar.

NOTE 5. LIQUID ASSETS

At December 31, 2016 and 2015, the item of liquid assets is summarized as follows:

	2016	2015
Deposits in the Banco de México	\$ 13,079	\$ 13,075
Deposits in domestic and foreign banks	13,242	6,178
Foreign currencies to deliver	(19,743)	(5,951)
Foreign currencies to receive	6,318	6,279
Call Money Deposits	2,800	934
Other liquid assets	1	4
Liquid assets in subsidiaries	1	1
	<u>\$ 15,698</u>	<u>\$ 20,520</u>

Deposits in Banco de México apply to monetary regulation deposits, in conformity with the telefax circular 1/2007 issued by Banxico on January 27, 2007.

At December 31, 2016, the Institution maintained Call Money deposits at a term less than or equal to three bank business days for \$2,800, of which \$73 were contracted at an average rate of 5.75% in local currency, as well as \$2,727 at an average rate of 0.68% in foreign currency.

At December 31, 2015, the Institution maintained Call Money deposits at a term less than or equal to three bank business days for \$934, of which \$675 were contracted at an average rate of 3.20% in local currency, as well as \$259 at an average rate of 0.55% in foreign currency.

Liquid assets in foreign currency at December 31, 2016 and 2015 are summarized as follows:

	Amount in millions of foreign currency	Exchange rate	Equivalence in local currency
2016			
US dollars	43	20.61940	\$ 879
Japanese yen	1	0.176810	-
Euros	3	21.75347	67
Pounds sterling	2	25.48145	47
			<u>\$ 993</u>
2015			
US dollars	387	17.24870	\$ 6,675
Japanese yen	4	0.14346	1
Euros	2	18.74934	30
Pounds sterling	2	25.43666	48
			<u>\$ 6,754</u>

NOTE 6. INVESTMENTS IN SECURITIES

As of December 31, 2016 and 2015, this item is summarized as shown below:

Trading securities:

Instrument	2016			2015	
	Cost of acquisition	Accrued interest	Valuation	Carrying value	Carrying value
Shares of the Development Fund for the Securities Market (DFSM)	\$ 109	\$ -	\$ (55)	\$ 54	\$ 96
Bonds	12,818	5	13	12,836	10,429
Securities exchange certificate	8,554	17	(10)	8,561	5,396
CETES	2,247	-	(2)	2,245	6
Ipabonos	2,862	32	16	2,910	14,200
Promissory notes with liquid yield at maturity	204	-	-	204	725
<i>Restricted financial instruments:</i>					
Bonds	88,239	24	-	88,263	33,329
Securities exchange certificate	14,223	3	(29)	14,197	10,078
CETES	230	-	-	230	-
Ipabonos	89,099	27	82	89,208	83,637
Promissory notes with liquid yield at maturity	1,500	-	1	1,501	3,375
<i>Financial instruments placed in guarantee:</i>					
Ipabonos	34	-	-	34	27
<i>Investments in subsidiaries</i>					
	18	-	-	18	-
	<u>\$ 220,137</u>	<u>\$ 108</u>	<u>\$ 16</u>	<u>\$ 220,261</u>	<u>\$ 161,298</u>

The terms at which these investments are agreed upon at December 31, 2016 and 2015 at their cost of acquisition are as follows:

<u>Instrument</u>	<u>Less than one month</u>	<u>Between one and three months</u>	<u>More than three months</u>	<u>No fixed term</u>	<u>Total</u>
2016					
Shares of the Development Fund for the Securities Market (DFSM)	\$ -	\$ -	\$ -	\$ 109	\$ 109
Bonds	9,389	-	3,429	-	12,818
Securities exchange certificate	3,211	-	5,343	-	8,554
CETES	2,236	4	7	-	2,247
Ipabonos	101	-	2,761	-	2,862
Promissory notes with liquid yield at maturity	204	-	-	-	204
<i>Restricted financial instruments:</i>	-	-	88,239	-	88,239
Bonds	-	-	-	-	-
Securities exchange certificate	14,223	-	-	-	14,223
CETES	230	-	-	-	230
Ipabonos	-	-	89,099	-	89,099
Promissory notes with liquid yield at maturity	1,500	-	-	-	1,500
<i>Financial instruments placed in guarantee:</i>	-	-	34	-	34
Ipabonos	-	-	34	-	34
Investments in subsidiaries	18	-	-	-	18
	<u>\$ 31,112</u>	<u>\$ 4</u>	<u>\$ 188,912</u>	<u>\$ 109</u>	<u>\$ 220,137</u>
2015					
Shares of the Development Fund for the Securities Market (DFSM)	\$ -	\$ -	\$ -	\$ 148	\$ 148
Bonds	6,227	-	4,191	-	10,418
Securities exchange certificate	-	-	5,388	-	5,388
CETES	4	-	2	-	6
Ipabonos	9,300	-	4,821	-	14,121
Promissory notes with liquid yield at maturity	725	-	-	-	725
<i>Restricted financial instruments</i>	33,538	-	-	-	33,538
Bonds	33,538	-	-	-	33,538
Securities exchange certificate	10,068	-	-	-	10,068
Ipabonos	83,662	29	-	-	83,691
Promissory notes with liquid yield at maturity	3,375	-	-	-	3,375
<i>Financial instruments placed in guarantee</i>	27	-	-	-	27
Ipabonos	27	-	-	-	27
	<u>\$ 146,926</u>	<u>\$ 29</u>	<u>\$ 14,402</u>	<u>\$ 148</u>	<u>\$ 161,505</u>

Available-for-sale securities:

At December 31, 2016 and 2015, liquid assets for sale are summarized in accordance with the following:

Instrument	2016			2015	
	Cost of acquisition	Accrued interest	Valuation	Carrying value	Carrying value
Sovereign debt	\$ 3,172	\$ 63	\$ (89)	\$ 3,146	\$ 2,064
Bonds issued by a Lending Institution	204	50	(2)	252	168
Debentures and other securities	3,548	-	(58)	3,490	2,909
	<u>\$ 6,924</u>	<u>\$ 113</u>	<u>\$ (149)</u>	<u>\$ 6,888</u>	<u>\$ 5,141</u>

The terms at which these investments are agreed upon at December 31, 2016 and 2015 at their cost of acquisition are as follows:

Instrument	More than one year	
	2016	2015
Sovereign debt	\$ 3,172	\$ 2,037
Bonds issued by a Lending Institution	204	171
Debentures and other securities	3,548	3,018
	<u>\$ 6,924</u>	<u>\$ 5,226</u>

Held-to-maturity securities

As of December 31, 2016 and 2015, medium and long-term debt securities are divided as follows:

Instrument	2016			2015	
	Cost of acquisition	Accrued interest	Carrying value	Carrying value	
Prides convertible bonds	\$ 5	\$ -	\$ 5	\$ 4	
Securities exchange certificate	268	70	338	126	
Segregable securities exchange certificate	1,167	387	1,554	5,635	
Sovereign debt	183	4	187	561	
Debentures and other securities	1,143	17	1,160	1,081	
Udibonos	51	16	67	209	

Instrument	2 0 1 6			2 0 1 5
	Cost of acquisition	Accrued interest	Carrying value	Carrying value
<i>Restricted financial instruments:</i>				
Segregable securities exchange certificate	7,175	2,385	9,560	5,308
Total	\$ 9,992	\$ 2,879	\$ 12,871	\$ 12,924

The terms at which these investments are agreed upon at December 31, 2016 and 2015 at their cost of acquisition are as follows:

Instrument	Less than one year	More than one year	No fixed term	Total
2 0 1 6				
Prides convertible bonds	\$ -	\$ 5	\$ -	\$ 5
Securities exchange certificate	268	-	-	268
Segregable securities exchange certificate	-	1,167	-	1,167
Sovereign debt	-	183	-	183
Debentures and other securities	87	1,056	-	1,143
Udibonos	-	51	-	51
<i>Restricted financial instruments:</i>				
Segregable securities exchange certificate	-	7,175	-	7,175
Total	\$ 355	\$ 9,637	\$ -	\$ 9,992

For the period extending from January 1 up to December 31, 2016, interest income on investments in securities amounted to \$1,725. The gain on valuation amounted to \$186, and the gain or loss on securities trading amounted to \$541.

Instrument	Less than one year	More than one year	No fixed term	Total
2 0 1 5				
Prides convertible bonds	\$ -	\$ -	\$ 4	\$ 4
Securities exchange certificate	-	98	-	98
Segregable securities exchange certificate	-	4,386	-	4,386
Sovereign debt	-	547	-	547
Debentures and other securities	-	1,037	-	1,037
Udibonos	114	51	-	165
<i>Restricted financial instruments:</i>				
Segregable securities exchange certificate	4,109	-	-	4,109
Total	\$ 4,223	\$ 6,119	\$ 4	\$ 10,346

For the period extending from January 1 up to December 31, 2015, interest income on investments in securities amounted to \$1,015. The gain on valuation amounted to \$314, and the gain or loss on securities trading amounted to \$111.

As of December 31, 2016 and 2015, there have been no reclassifications of securities held to maturity securities available for sale, or securities held to trade available for sale.

NOTE 7. REPURCHASE TRANSACTIONS

At December 31, 2016 and 2015, repurchase transactions (repos) are summarized as follows:

Instrument	Received in guarantee	Collateral received and sold or furnished as a guarantee	Difference
2016			
Governmental securities:			
CETES	\$ 20	\$ -	\$ 20
Ipabonos	5,934	5,934	-
Federal Government Development Bonds (Bondes)	16,331	16,331	-
Fixed rate bonds	12	12	-
	\$ 22,297	\$ 22,277	\$ 20
2015			
Governmental securities:			
Udibonos	\$ 63	\$ -	\$ 63
Ipabonos	3,941	3,941	-
Federal Government Development Bonds (Bondes)	27,994	27,744	250
Fixed rate bonds	4,556	4,556	-
	\$ 36,554	\$ 36,241	\$ 313

At those same dates, the borrowing party of payables under repurchase agreements are as follows:

	2016	2015
Governmental securities:		
Bonds	\$ 88,262	\$ 33,541
Segregable securities exchange certificate	9,344	5,096
CETES	230	-
Ipabonos	89,127	83,709
	186,963	122,346
Bank securities:		
Securities exchange certificate	14,226	10,070
Promissory notes with liquid yield at maturity	1,500	3,376
	15,726	13,446
	\$ 202,689	\$ 135,792

For the year extending from January 1 up to December 31, 2016, the gain or loss on interest income and expense on repurchase transactions amounts to \$10,097 and \$9,057, respectively, and income amounting to \$7,880 and expenses amounting to \$6,328 in 2015.

The contracting terms in repurchase transactions realized by the institution are from 1 to 180 days.

NOTE 8. DERIVATIVES

At December 31, 2016 and 2015, the Institution maintains balances in derivative instruments trading as described below:

	<u>Lending balance</u>	<u>Borrowing balance</u>	<u>Debit balance</u>	<u>Credit balance</u>
2016				
<i>For trading purposes:</i>				
Futures	\$ 2	\$ 2	\$ -	\$ -
Valuation	-	-	-	-
	<u>2</u>	<u>2</u>	-	-
<i>For trading purposes:</i>				
Forward contracts	\$ 64,023	\$ 64,069	\$ (46)	\$ -
Valuation	(35)	(263)	228	-
	<u>63,988</u>	<u>63,806</u>	<u>182</u>	<u>-</u>
Swaps	54,460	54,511	-	51
Total	<u>\$ 118,450</u>	<u>\$ 118,319</u>	<u>\$ 182</u>	<u>\$ 51</u>
<i>For hedging purposes:</i>				
Swaps	<u>\$ 33,728</u>	<u>\$ 43,232</u>	<u>\$ -</u>	<u>\$ 9,504</u>
2015				
<i>For trading purposes:</i>				
Futures	\$ 468	\$ 468	\$ -	\$ -
Valuation	-	(1)	1	-
	<u>468</u>	<u>467</u>	<u>1</u>	<u>-</u>
<i>For trading purposes:</i>				
Forward contracts	\$ 15,093	\$ 14,939	\$ 154	\$ -
Valuation	(2)	(16)	14	-
	<u>15,091</u>	<u>14,923</u>	<u>168</u>	<u>-</u>
Swaps	53,430	53,421	9	-
Total	<u>\$ 68,989</u>	<u>\$ 68,811</u>	<u>\$ 178</u>	<u>\$ -</u>
<i>For hedging purposes:</i>				
Swaps	<u>\$ 26,786</u>	<u>\$ 29,109</u>	<u>\$ -</u>	<u>\$ 2,323</u>

Future and forward contracts (Forward):

For trading purposes

Swaps:*For trading purposes:*

	<u>Contract value</u>	<u>Receivable</u>	<u>Deliverable</u>	<u>Net position</u>
2016				
Interest rates	\$ 133,392	\$ 54,460	\$ 54,511	\$ (51)
2015				
Interest rates	\$ 141,530	\$ 53,430	\$ 53,421	\$ 9

For hedging purposes:

	<u>Contract value</u>	<u>Receivable</u>	<u>Deliverable</u>	<u>Net position</u>
2016	\$ 81,016	\$ 33,728	\$ 43,232	\$ (9,504)
2015	\$ 68,810	\$ 26,786	\$ 29,109	\$ (2,323)

At December 31, 2016 and 2015, hedge effectiveness/ineffectiveness derived from the application of Criterion B-5 "Derivatives and Hedging Transactions" of the Commission is described in detail below:

Fair value hedge swaps (applicable to income):

	<u>2016</u>	<u>2015</u>
Valuation of:		
Securities exchange certificate	\$ (48)	\$ (35)
Certificates of deposit	6	7
Total	\$ (42)	\$ (28)

At December 31, 2016 and 2015, the Institution has only contracted swaps designated as fair value hedges.

Trading swaps (application to income):

	<u>2016</u>	<u>2015</u>
Interest rates	\$ (51)	\$ 9

The adjustments at carrying value from trades derived from interest rate hedges of financial assets and liabilities due to the application of Criterion B-5 "Derivatives and Hedge Trading" of the Commission at December 31, 2016 and 2015 are described in detail below:

	2016		2015	
	Assets	Liabilities	Assets	Liabilities
Securities exchange certificate	\$ (5,291)	\$ (8,256)	\$ (490)	\$ (435)
Promissory notes	(55)	(60)	7	7
Loan	5,417	4,617	1,797	1,536
Total	\$ 71	\$ (3,699)	\$ 1,314	\$ 1,108

Management of the policies of the use of derivative financial instruments

The Institution's policies permit the use of derivative products for hedging and/or trading purposes. The main objective of trading these products is the hedging of risks and generation of revenues that support the Institution's profitability.

Setting objectives and policies related to trading these instruments is in the Risk Management regulatory and operating manuals.

The instruments used by the Institution are interest and exchange rate swaps, IPC futures and exchange rates, and foreign exchange forwards, which, in accordance with the portfolios, can support hedging and trading strategies.

The markets on which derivative products are traded are the OTC (over-the-counter) markets and stock markets. Eligible counterparties are domestic and foreign banks, whereas stock exchange firms are clearing houses.

Authorization processes and levels

Control processes, policies, and authorization levels of derivatives trading are set forth in the CAIR, whose duties include the approval of:

1. The specific limits for discretionary risks when powers have been delegated by the Board of Directors therefor, as well as the levels of tolerance in the case of non-discretionary risks.
2. The methodology and procedures for identifying, measuring, overseeing, limiting, controlling, reporting, and disclosing the distinct types of risk that the Institution is exposed to as well as their eventual modifications.
3. The models, parameters and scenarios that must be used to value, measure, and control the risks proposed by the unit for Comprehensive Risk Management, must concur with the institution's technology.
4. The methodologies for identifying, valuing, measuring, and controlling the risks of the new operations, products, and services that the Institution plans to offer to the market.
5. The corrective actions proposed by the unit for Comprehensive Risk Management.

6. The evaluation of the aspects of Comprehensive Risk management referred to in Article 77 of the Provisions for its presentation to the Board of Directors and the Commission.
7. The Comprehensive Risk Management manuals, in accordance with the objectives, guidelines, and policies established by the Board of Directors, referred to in the last paragraph of Article 78 of the Provisions.

All the new products or services traded in reliance on any line of business are approved by the Committee, in accordance with the powers granted by the Board of Directors.

Independent reviews

The Institution is under the supervision and oversight of the Commission and the Banco of México, which are exercised through follow-up processes, inspection visits, information and documentation requirements, and delivery of reports. Moreover, reviews are performed periodically by the internal and external auditors.

Generic description of valuation techniques

Derivative financial instruments are valued in conformity with the accounting regulations set forth in the Provisions issued by the Commission, due particularly to the standard contained in Criterion B-5.

Valuation methodology

1. For purposes of trades and hedges - there is a structure of operating and regulatory manuals that set forth the valuation methodologies used.
2. Reference variables. Those parameters are used that are utilized by convention within the market practices (rates, exchange rates, prices, volatilities, etc.).
3. Frequency of valuation - Trading position instruments are valued every day.

Administration of internal and external sources of liquidity that might be used to meet requirements related to derivative financial instruments

Resources obtained through the National Treasury, as well as the international Treasury (London Branch).

Changes identified in risk exposure, contingencies, and known or expected events in derivative financial instruments.

Stress tests and backtesting are realized periodically to estimate the impact on the positions of derivative instruments and satisfactorily validate that the market risk measurement models provide results, in accordance with the exposure to market variability, which must be maintained within the parameters authorized by the CAIR.

The methodology currently used for preparing the stress measurement report consists of calculating the current portfolio value, and be able to make changes in the risk factors that occurred in the:

- Tequila Effect (1994)
- Russian Crisis (1998)
- Twin Towers (2001)
- BMV Effect (2002)
- Effect on Real Interest Rate (2004)
- Mortgage Crisis Effect (2008)

Backtests are based on the following information generated daily:

1. Valuation of the investment portfolio of the day t
2. The VaR of the investment portfolio with a 1 day time horizon and with a level of confidence of 97.5% (VaR).
3. The valuation of the portfolio with the new risk factors of the day t+1

During 2016, the number of derivative financial instruments agreed upon was as follows:

Instrument		Number of Operations		Notional	
		Trade	Hedge	Trade	Hedge
Futures	(1)	3,378		121,598	
Forwards (Arbitrations)	(2)	378		46,036	
Swaps	(3)	87	124	17,742	28,678

- (1) Number of trades is equal to the buy trades less sales trades. Notional refers to the number of contracts: 62,488 purchase and 59,110 sales.
- (2) Purchase transactions. Notional in millions of US dollars
- (3) Notional amount traded during the year.

Formal documentation of hedges

In order to comply with the applicable regulations with respect to derivatives and hedging transactions (Criterion B-5 issued by the Commission), the Institution has a hedge file that includes the following information:

1. File cover.
2. Authorization of the hedge.
3. Diagram of the strategy.
4. Evidence of prospective tests of hedge effectiveness.
5. Evidence of execution of the derivative.
6. Details of the primary position being hedged.
7. Confirmation of the derivative.

Sensitivity analysis

A sensitivity analysis is realized through distinct measures every day, such as:

1. **Duration.**- There are primarily two types of duration with different meanings:
 - a) Macaulay Duration: It is the weighted average maturity of the current cash flow values where weighting ratios are the time in years up to the payment of the corresponding flow.
 - b) Modified Duration: It is the variation by percentage experienced by the price of a small bond before small variations in the market interest rate.
2. **Convexity.**- It is the variation experienced by the slope of a curve with respect to a dependent variable or what is the same, it measures the variation experienced, as well as the duration before changes in rates.
3. **Greeks.**- Sensitivity measurements for options, except for interest rate options:
 - a) Delta: Price sensitivity of options at the price of the underlying securities of the option.
 - b) Theta: Price sensitivity of options to the variable time.
 - c) Gamma: Third degree price sensitivity of the option to the underlying securities of the option.
 - d) Vega: Price sensitivity of the option to the volatility used for its valuation.
 - e) Rho: Price sensitivity of the option to changes in the interest rate.
4. **Beta.**- It is the measurement of the systematic risk of a share.

This analysis is reported to the instances that define the operating strategy of derivatives on financial markets and operators therein, in order for it to govern its criterion in taking the risk with these instruments.

NOTE 9. LOAN PORTFOLIO

As of December 31, 2016 and 2015, the portfolio by type of loan is summarized as shown below:

	<u>2016</u>	<u>2015</u>
Performing portfolio:		
Business or commercial activity credits	\$ 59,882	\$ 38,857
Loans to financial entities	134,329	119,788
Loans to government entities	17,688	10,901
Consumer lending	8	7
Mortgage loans	134	146
Federal Government financial agent	94	109
	<u>212,135</u>	<u>169,808</u>
Nonperforming portfolio:		
Business or commercial activity credits	602	6
Loans to financial entities	1,560	1,870
Consumer lending	4	4
Mortgage loans	12	14
	<u>2,178</u>	<u>1,894</u>
Total	\$ <u>214,313</u>	\$ <u>171,702</u>

The nonperforming portfolio presents an increase amounting to \$284, caused mainly by the book transfer derived from Metalwork & Stamping, S.A. de C.V.

At those same dates, the loan portfolio by source currency is summarized as follows:

	<u>2016</u>		<u>2015</u>	
	<u>Performing</u>	<u>Nonperforming</u>	<u>Performing</u>	<u>Nonperforming</u>
Local Currency	\$ 161,635	\$ 1,575	\$ 134,386	\$ 1,894
Foreign Currency	50,500	603	35,422	-
Total	<u>\$ 212,135</u>	<u>\$ 2,178</u>	<u>\$ 169,808</u>	<u>\$ 1,894</u>

Credits granted as a Financial Agent apply to financing granted to Federal Government entities with resources obtained from international agencies for that specific purpose. They are presented in an independent item of the loan portfolio.

Credits to financial entities are granted to banking and non-banking entities, through the discount of notes payable by legal entities and sole proprietors engaged in business activities.

At December 31, 2016, the Institution does not report credit indebtedness subject to Support Programs promoted by the Federal Government.

The balance of the nonperforming portfolio at December 31, 2016 and 2015 in a total amount of \$2,178 and \$1,894, respectively, since the date on which it was classified as nonperforming, is described in detail below:

	<u>Capital and interest</u>	<u>Amounts</u>	<u>Terms</u>
2016			
Business or commercial activity credits	\$ 602	\$ 602	More than 2 years
Loans to financial entities	1,560	1,560	More than 2 years
Consumer lending	4	1	1 to 180 days
Consumer lending	-	1	181 to 365 days
Consumer lending	-	2	More than 2 years
Mortgage loans	12	2	1 to 180 days
Mortgage loans	-	10	More than 2 years
	<u>\$ 2,178</u>	<u>\$ 2,178</u>	
2015			
Business or commercial activity credits	\$ 6	\$ 6	More than 2 years
Loans to financial entities	1,870	1,870	More than 2 years
Consumer lending	4	1	1 to 180 days
Consumer lending	-	3	More than 2 years
Mortgage loans	14	2	1 to 180 days
Mortgage loans	-	12	More than 2 years
	<u>\$ 1,894</u>	<u>\$ 1,894</u>	

Nonperforming portfolio movements are presented below:

	<u>2016</u>	<u>2015</u>
Balances at January 1	\$ 1,894	\$ 1,892
Payments	(337)	-
Reclassification to nonperforming portfolio	621	2
Total	<u>\$ 2,178</u>	<u>\$ 1,894</u>

At December 31, 2016 and 2015, the balance of the nonperforming portfolio consists of 69 former employees, and 16 companies, which are in legal or out-of-court proceedings.

Loan portfolio interest and fees at December 31, 2016 and 2015 are summarized as itemized below:

	<u>Interest</u>	<u>Fees on credit granted</u>	<u>Total</u>
2016			
Business or commercial activity credits	\$ 2,114	\$ 39	\$ 2,153
Loans to financial entities	6,014	55	6,069

	<u>Interest</u>	<u>Fees on credit granted</u>	<u>Total</u>
Loans to government entities	716	-	716
Mortgage loans	2	-	2
Federal Government financial agent	3	-	3
	<u>\$ 8,849</u>	<u>\$ 94</u>	<u>\$ 8,943</u>

2015

Business or commercial activity credits	\$ 1,454	\$ 48	\$ 1,502
Loans to financial entities	4,267	46	4,313
Loans to government entities	392	-	392
Mortgage loans	1	-	1
Federal Government financial agent	12	-	12
	<u>\$ 6,126</u>	<u>\$ 94</u>	<u>\$ 6,220</u>

The effect derived from the suspension of the accrual of interest of the nonperforming portfolio represented a decrease amounting to \$107 compared to 2015, derived from adjustments to balances recognized due to borrowers that went into commercial bankruptcy.

Fees collected do not have associated costs and expenses. Moreover, the weighted average term for amortization of fees collected for granting the initial credit is monthly.

At December 31, 2016 and 2015, restructured loans are summarized as follows:

	<u>Performing</u>	<u>Nonperforming</u>	<u>Total</u>
2016			
Business or commercial activity credits	\$ 47	\$ -	\$ 47
Financial entities	280	-	280
	<u>\$ 327</u>	<u>\$ -</u>	<u>\$ 327</u>
2015			
Business or commercial activity credits	\$ 47	\$ 1	\$ 48
Financial entities	360	254	614
Housing	-	1	1
	<u>\$ 407</u>	<u>\$ 256</u>	<u>\$ 663</u>

At December 31, 2016 and 2015, restructured interest income amounts to \$18 in both years.

At December 31, 2016 and 2015, the percentage of concentration of the portfolio by sector is as follows:

	Percentage (%)	
	2016	2015
Federal Government	0.06	0.09
Decentralized agencies and state-owned enterprises	4.07	2.94
State productive enterprises	3.04	2.62
Development banking	-	0.06
Commercial banks	24.90	33.86
Other public financial brokers	1.13	0.76
Other private financial brokers	41.10	36.66
Domestic companies	25.42	22.64
Private parties	0.07	0.10
Foreign financial entities	0.21	0.27
Total	100.00	100.00

In accordance with Criterion B-6 "Loan Portfolio" of the Provisions, all those commercial credits are understood as impaired portfolio. Based on current information and events, as well as the review process of such credits, there is a considerable likelihood that both the principal component and interest of impaired portfolio may not be entirely recovered, in accordance with the terms and conditions agreed upon originally. Both the current portfolio and nonperforming portfolio may be identified as an impaired portfolio.

At December 31, 2016 and 2015, the following has been recognized as impaired commercial portfolio:

	Degree of risk			Legal created
	D	E	Total	
2016				
Performing	\$ 47	\$ -	\$ 47	\$ 21
Nonperforming	-	2,163	2,163	1,496
Total	\$ 47	\$ 2,163	\$ 2,210	\$ 1,517
2015				
Performing	\$ 47	\$ -	\$ 47	\$ 21
Nonperforming	-	1,711	1,711	1,373
Total	\$ 47	\$ 1,711	\$ 1,758	\$ 1,394

NOTE 10. ALLOWANCE FOR LOAN LOSSES

In accordance with the Rules for Rating the Loan Portfolio for Development Banking Institutions, the loan portfolio under the responsibility of the Federal Government and taking a discount from development banking institutions is not subject to the creation of allowances, since these entities assume the credit risk. The balance of the loan portfolio and that of contingent operations subject to a rating are controlled in memorandum accounts and evaluated based on the methodologies established by the Commission. The allowances for loan losses recorded at December 31, 2016 and 2015 is summarized as follows:

	Risk	Amount of liabilities	Estimate of the provision
2016			
	A-1	\$ 189,045	\$ 1,110
	A-2	54,211	602
	B-1	19,018	333
	B-2	8,194	180
	B-3	4,796	174
	C-1	238	14
	C-2	19	2
	D	115	42
	E	2,192	1,517
Rated portfolio		<u>277,828</u>	<u>3,974</u>
Exempted portfolio:			
Federal Government		94	-
Additional estimates		-	865
Estimate for assignment of lines		-	800
		<u>\$ 277,922</u>	<u>\$ 5,639</u>
2015			
	A-1	\$ 128,952	\$ 682
	A-2	71,573	823
	B-1	23,444	436
	B-2	2,104	48
	B-3	2,681	97
	C-1	589	35
	C-2	73	9
	D	96	32
	E	1,731	1,388
Rated portfolio		<u>231,243</u>	<u>3,550</u>
Exempted portfolio:			
Federal Government		109	-
Additional estimates		-	753
Estimate for assignment of lines		-	400
		<u>\$ 231,352</u>	<u>\$ 4,703</u>

Percentage of Allowances for Loan Losses

Degree of risk	Consumer			
	Non-revolving	Credit card and other revolving credits	Mortgage and housing	Commercial
A - 1	0 to 2.0	0 to 3.0	0 to 0.50	0 to 0.9
A - 2	2.01 to 3.0	3.01 to 5.0	0.501 to 0.75	0.901 to 1.5
B - 1	3.01 to 4.0	5.01 to 6.5	0.751 to 1.0	1.501 to 2.0
B - 2	4.01 to 5.0	6.51 to 8.0	1.01 to 1.50	2.01 to 2.50
B - 3	5.01 to 6.0	8.01 to 10.0	1.501 to 2.0	2.501 to 5.0
C - 1	6.01 to 8.0	10.01 to 15.0	2.01 to 5.0	5.001 to 10.0
C - 2	8.01 to 15.0	15.01 to 35.0	5.001 to 10.0	10.001 to 15.5
D	15.01 to 35.0	35.01 to 75.0	10.001 to 40.0	15.501 to 45.0
E	35.01 to 100.0	Higher than 75.01	40.001 to 100.0	Higher than 45.0

At December 31, 2016 and 2015, the amount of \$339 was reduced from the commercial portfolio rated with an E risk rating, for which the corresponding allowance for loan losses was not created since collateral has received in cash at the Institution. In the accounting records, it is presented as a credit portfolio in the respective degree of risk, in both years.

At December 31, 2016 and 2015, the preventive estimate for credit risks amounts to \$54, which corresponds to the total interest in arrears account.

At those same dates, the preventive estimate for credit risks by type of credit is summarized as follows:

	<u>2016</u>	<u>2015</u>
Specific estimates:		
Loan portfolio:		
Business or commercial activity credits	\$ 796	\$ 370
Loans to financial entities	2,666	2,768
Loans to government entities	89	59
Consumer lending	4	5
Mortgage loans	9	11
	<u>3,564</u>	<u>3,213</u>
Contingent portfolio:		
Guarantees by endorsement executed	36	32
Guarantees furnished	374	305
Additional estimates	865	753
Estimate for assignment of lines	800	400
Total	<u>\$ 5,639</u>	<u>\$ 4,703</u>

The movements of the preventive estimate for credit risks are presented below:

	<u>2016</u>	<u>2015</u>
Balances at January 1	\$ 4,703	\$ 3,955
<i>Increases:</i>		
Discounts on recovery of debts	-	-
Creation of reserves for credit risks	1,532	1,253
Slippage of the foreign currency reserve	131	44
	<u>1,663</u>	<u>1,297</u>
<i>Applications:</i>		
Discounts on recovery of debts	2	2
Reversal of surplus reserves	146	547
Write-off of credit debts	579	-
Total	<u>\$ 5,639</u>	<u>\$ 4,703</u>

NOTE 11. OTHER RECEIVABLES, NET

At December 31, 2016 and 2015, other receivables are shown as follows:

	<u>2016</u>	<u>2015</u>
Loans to Institution personnel	\$ 2,489	\$ 2,379
Clearing accounts	13,424	179
Other receivables	62	32
Receivables for fees on current trading activities	93	76
Other receivables from subsidiaries	258	189
Payments receivable on swap trades	9,618	2,315
Estimates for write-offs of other receivables	(47)	(28)
Total	<u>\$ 25,897</u>	<u>\$ 5,142</u>

NOTE 12. REPOSSESSED ASSETS, NET

At December 31, 2016 and 2015, repossessed assets are summarized as follows:

	<u>2016</u>	<u>2015</u>
Real property	\$ 31	\$ 26
Securities	32	42
	<u>63</u>	<u>68</u>
Allowances (provisions) for write-offs	(54)	(51)
Total	<u>\$ 9</u>	<u>\$ 17</u>

Write-offs relative to repossessed assets recorded in income at December 31, 2016 and 2015 amount to \$3 and \$7, respectively.

In conformity with the Provisions, additional allowances (provisions) have been recognized for holding repossessed assets or out-of-court proceedings or received as a dation in payment.

NOTE 13. PROPERTY, FURNITURE AND EQUIPMENT, NET

At December 31, 2016 and 2015, property, plant and equipment are summarized as follows:

Item	2016			2015
	Investment			Total
	Historical	Restatement	Total	
Building	\$ 300	\$ 1,941	\$ 2,241	\$ 2,269
Furniture and equipment	147	96	243	234
Computer equipment	21	9	30	27
Land	9	-	9	13
Subtotal	477	2,046	2,523	2,543
Accumulated depreciation	(233)	(788)	(1,021)	(991)
Total	\$ 244	\$ 1,258	\$ 1,502	\$ 1,552

Useful lives during which the main assets are depreciated are shown below:

Item	Useful life
Building	53 to 70 years
Furniture and equipment	10 years
Computer equipment	3 to 4 years

Depreciation expensed in 2016 and 2015 amounted to \$38 and \$35, respectively.

NOTE 14. OTHER INVESTMENTS

At December 31, 2016 and 2015, other permanent investments are summarized as shown below:

	2016	2015
Technical Assistance S&ME Financing Programs Trust	\$ 16	\$ 9
México Design Center Sponsorship Trust	15	17
Venture Capital Trust	4	3
Trust placed on Intermediate Securities Market	3	3
Eurocentro Nafin-México Trust	1	1
Total	\$ 39	\$ 33

NOTE 15. PERMANENT INVESTMENTS

At December 31, 2016 and 2015, stock in permanent investments is summarized as shown below:

	<u>2016</u>	<u>2015</u>
Corporación Andina de Fomento	\$ 2,692	\$ 2,289
Shares of other companies	133	33
	<u>2,825</u>	<u>2,322</u>
Investment of subsidiary companies:	6,692	5,222
Total	<u>\$ 9,517</u>	<u>\$ 7,544</u>

NOTE 16. TERM DEPOSITS

At December 31, 2016 and 2015, the terms to maturity of these securities are as follows:

	<u>2016</u>	<u>2015</u>
Less than one year	\$ 143,075	\$ 118,335
Five years	153	7,152
	<u>143,228</u>	<u>125,487</u>
Unpaid accrued interest	242	247
	<u>\$ 143,470</u>	<u>\$ 125,734</u>

NOTE 17. NEGOTIABLE INSTRUMENTS ISSUED IN THE COUNTRY

The balance of this item consists of stock certificates (CEBURES) as follows:

<u>Inception</u>	<u>Expiration</u>	<u>Securities (millions)</u>	<u>Face value (pesos)</u>	<u>% Rate</u>	<u>2016</u>	<u>2015</u>
CEBURES Payable at Indeal:						
11/22/2013	11/18/2016	20	100	3.27	\$ -	\$ 2,000
03/14/2014	11/18/2016	12.5	100	3.27	-	1,250
08/03/2012	07/22/2022	20	100	5.69	2,000	2,000
12/10/2012	07/22/2022	20	100	5.69	2,000	2,000
11/22/2013	03/08/2024	30	100	6.55	3,000	3,000
03/14/2014	03/08/2024	47.5	100	6.55	4,750	4,750
06/06/2014	06/02/2017	20	100	3.24	2,000	2,000
06/06/2014	03/08/2024	40	100	6.55	4,000	4,000

Inception	Expiration	Securities (millions)	Face value (pesos)	% Rate	2 0 1 6	2 0 1 5
09/26/2014	06/02/2017	17.5	100	3.24	1,750	1,750
09/26/2014	03/08/2024	32.5	100	6.55	3,250	3,250
04/17/2015	03/07/2025	60	100	6.15	6,000	6,000
04/17/2015	04/13/2018	10	100	3.23	1,000	1,000
08/24/2015	04/13/2018	30	100	3.48	3,000	3,000
08/24/2015	03/07/2025	40	100	6.15	4,000	4,000
Premium or discount on placement					(35)	(39)
Accrued interest payable					571	569
					<u>37,286</u>	<u>40,530</u>
CEBURES payable at Euroclear and Clearstream						
04/25/2016	04/17/2019	10	100	4.05	1,000	-
04/27/2016	09/25/2026	50	100	6.20	5,000	-
10/21/2016	04/17/2019	18	100	5.52	1,800	-
10/25/2016	09/25/2026	42	100	6.20	4,200	-
Premium or discount on placement					(94)	-
Accrued interest payable					135	-
					<u>12,041</u>	<u>-</u>
Green bond denominated in Local Currency						
09/02/2016	09/01/2023	20	100	6.05	2,000	-
Accrued interest payable					40	-
					<u>2,040</u>	<u>-</u>
Total					\$ <u>51,367</u>	\$ <u>40,530</u>

Two stock certificates (fixed rate and reviewable rate) were issued under the communicative units format in April 2016, and in reliance on the program of syndicated auctions that the Institution has been carrying out since the end of 2013. However, there was a new characteristic for the fixed rate tranche, since the necessary formalities were carried out for that instrument to be settled through Euroclear or Clearstream. This permits the participation of foreign investors in the local issue and seeks to increase the base of investors. The foregoing is highlighted by the foreign participation obtained for the first time, mainly through European banks. That instrument was reopened successfully in October, which was also carried out with the characteristic that it can be settled through Euroclear and Clearstream.

In addition, the Institution issued its second Green Bond in November 2016, through a transaction on the local market denominated in pesos with a seven year term. The placement was well diversified with investors, which positioned the Institution again as a leading development bank in this type of initiatives to promote the transition toward a competitive, sustainable economy with low emissions. The demand was close to 6 billion pesos (2.92 times), and the final placement amounted to 2 billion pesos, which will initially be used of financing three projects, two hydroelectric mini-plants, and an eolian park located in Nayarit and Puebla, respectively. The issue was also highlighted by the support obtained of the second opinion of Sustainalytics. This marks the beginning of Green Bonds in México, since it is the first issue in pesos of this type in México.

NOTE 18. NEGOTIABLE INSTRUMENTS ISSUED ABROAD

Bank bonds:

At December 31, 2016 and 2015, the balances of this item amount to \$28,622 and \$19,660, respectively.

The current balances of securities placed by the Institution abroad are presented in this item, which is summarized as follows:

Currency	Securities	Source currency		% Average rate	Balance in local currency	Term
		Value	Interest			
2 0 1 6						
US dollars	87	1,237	2	1.05351	\$ 25,544	less than one year
Euros	4	149	-	1.64825	3,078	more than one year
					<u>\$ 28,622</u>	
2 0 1 5						
US dollars	54	1,127	2	0.53976	\$ 19,473	less than one year
Euros	1	10	-	0.03000	187	less than one year
					<u>\$ 19,660</u>	

Marketable Notes:

At December 31, 2016 and 2015, the balance in this item amounting to \$10,352 and \$8,655, respectively, is summarized as follows:

Currency	Source currency		% Rate	Balance in local currency	Term
	Value	Interest			
2016					
US dollars	500	3	3.37500	\$ <u>10,352</u>	5 years
2015					
US dollars	500	3	3.37500	\$ <u>8,655</u>	5 years

The Institution issued the first Mexico's "Green Bond" for USD 500 million over a five year term at a fixed coupon rate of 3.375% in 2015, thereby marking its return to the international financial markets after an 18 year absence. The transaction had a demand exceeding USD 2 billion 500 million, which oversubscribed more than five times to one of the total amount placed, and a loan book of 60 international investors, which improves the liquidity gaps in the balance sheet in foreign currency, and computes in recognized indexes on international markets. This issue had the support of Sustainalytics B.V., an environmental, social, and governance (ESG) research and analysis provider, as well as the Climate Bond Certification internationally recognized certification issued by the Climate Bond Initiative. Moreover, this bond highlighted Mexico's commitment in being one of the main world promoters of sustainable development and promoting appropriate measures against climate change, thereby reaffirming its leadership as the first development bank in Latin America to issue a bond of this type. It is important to note that the total proceeds will be allocated exclusively to financing renewable energy projects (eolian parks).

NOTE 19. INTERBANK LOANS AND LOANS FROM OTHER AGENCIES

This item consists mainly of credits received from foreign financial institutions at current market or preferential based. Their analysis based is as follows:

	<u>2016</u>	<u>2015</u>
Multinational and governmental agencies		
World Bank	\$ 1,031	\$ 863
Inter-American Development Bank	7,540	7,274
Others	5,904	2,985
	<u>14,475</u>	<u>11,122</u>
Banking institutions	10,143	12,531
Other loans	5,699	55
Unpaid accrued interest	33	41
	<u>\$ 30,350</u>	<u>\$ 23,749</u>

At December 31, 2016 and 2015, maturities at a term less than one year amount to \$19,039 and \$14,030, respectively.

At December 31, 2016, interbank loans and from other agencies are summarized as follows:

Financial Agency	Average rate	Average term to maturity (residual)	Millions in source currency	Local currency
Demand deposits				
<i>Local Currency:</i>	5.7167	1 day	5,699	\$ 5,699
Interest			1	1
Total			<u>5,700</u>	<u>\$ 5,700</u>
Short-term				
<i>US dollars:</i>				
Commercial banking	1.3646	53 days	355	\$ 7,306
NF BID Cclip 2226 oc Me Development	2.1400	161 days	5	103
Official Institute of Credit	1.3333	120 days	1	21
Corporación Andina de Fomento	1.1004	31 days	280	5,773
			<u>641</u>	<u>\$ 13,203</u>
<i>Euros:</i>				
Commercial banking	1.4588	341 days	3	\$ 71
			<u>3</u>	<u>\$ 71</u>
Financial Broker				
<i>Euros:</i>				
Inter-American Development Bank Washington, D.C.	3.0000	112 days	1	\$ 19
			<u>1</u>	<u>\$ 19</u>
<i>Special Draft fees:</i>				
International Agricultural Development Fund	27.7193	212 days	-	14
			<u>-</u>	<u>\$ 14</u>
Interest				
			<u>2</u>	<u>\$ 32</u>
			<u>2</u>	<u>\$ 32</u>
Total			<u>647</u>	<u>\$ 13,339</u>
Long-term				
<i>US dollars:</i>				
Commercial banking	20.6194	5 years	42	\$ 862
Official Institute of Credit	20.6194	6 months	77	1,595
NF BID Cclip 2226 oc Me Pemex S&ME Development	20.6194	9 years	88	1,804
NF ctf BIRF 98062 Electrodomestic Substitution Program	20.6194	18 years	50	1,031
2631 tc Me Renewable Energy Financing Program	20.6194	6 months	70	1,443
		13 years		
		9 months		
		15 years		
		7 months		

Financial Agency	Average rate	Average term to maturity (residual)	Millions in source currency	Local currency
NF BID Cclip 2843/oc-Me Condition Credit Line Program me-x1010	20.6194	21 years 5 months	100	2,062
NF BID 3237/oc-Me Co-generation Financing Stimulus Program	20.6194	23 years 6 months	100	2,062
			<u>527</u>	<u>\$ 10,859</u>
<i>Euros:</i>				
Commercial banking	1.4220	6 years	18	\$ 391
			<u>18</u>	<u>\$ 391</u>
Financial Broker				
<i>Euros:</i>				
Inter-American Development Bank Washington, D.C.	3.0000	2 years 4 months	2	\$ 47
			<u>2</u>	<u>\$ 47</u>
<i>Special Draft fees:</i>				
International Agricultural Development Fund	27.7193	1 year 8 months	-	\$ 14
			<u>-</u>	<u>\$ 14</u>
Total			<u>547</u>	<u>\$ 11,311</u>

At Thursday, December 31, 2015, interbank loans and from other agencies are summarized as follows:

Financial Agency	Average rate	Average term to maturity (residual)	Millions in source currency	Local currency
Short-term:				
<i>Local Currency</i>	3.22000	15 days	-	\$ 8,000
<i>Euros</i>	2.00000	182 days	1	11
<i>US dollars:</i>				
Commercial banking	0.91555	77 days	175	3,019
NF BID Cclip 2226 oc Me Pemex S&ME Development	1.52000	350 days	5	86
Corporación Andina de Fomento	0.83002	63 days	165	<u>2,845</u>
				<u>5,950</u>
Financial Broker				
<i>Euros:</i>				
Inter-American Development Bank Washington, D.C.	3.00000	290 days	1	16
<i>Special draft fees</i>	1.16000	213 days	-	12
Interest			-	<u>41</u>
Total				<u>\$ 14,030</u>

6.49

<u>Financial Agency</u>	<u>Average rate</u>	<u>Average term to maturity (residual)</u>	<u>Millions in source currency</u>	<u>Local currency</u>
Long-term:				
<i>US dollars:</i>				
NF BID Cclip 2226 oc Me Pemex S&ME Development	1.52000	19 years 6 months	93	1,596
NF ctf BIRF 98062 Electrodomestic Substitution Program	0.75000	14 years 9 months	50	862
NF BID 2671 Oc Me Unemployment Support Program of Mexico	1.52000	21 years	50	862
2631 tc Me Renewable Energy Financing Program	0.75000	16 years 7 months	70	1,207
NF BID Cclip 2843/oc-Me Condition Credit Line Program me-x1010	1.52000	22 years 4 months	100	1,725
NF BID 3237/ocOC-ME Co-generation E. Financing Stimulus Program	1.52000	24 years 5 months	100	1,725
Others	1.54773	5 years 5 months	69	1,200
<i>Euros</i>	1.42200	8 years	23	462
				<u>9,639</u>
Financial Broker				
<i>Euros:</i>				
Inter-American Development Bank Washington, D.C.	3.00000	4 years 4 months	3	57
<i>Special draft fees</i>	1.16000	2 years 8 months	1	23
Total			\$	<u>9,719</u>

The accounts of credits obtained not yet drawn down (Note 28) represents the lines of credit granted to the Institution not exercised at year end, as itemized below:

	<u>2016</u>	<u>2015</u>
Banco de México	\$ 535	\$ 499
Kreditanstalt Fur Wiederaufbau Frankfurt	701	604
Inter-American Development Bank	1,769	5,792
Subsidiaries	-	664
Total	<u>\$ 3,005</u>	<u>\$ 7,559</u>

NOTE 20. OTHER PAYABLES

At December 31, 2016 and 2015, this item consists of the following reserves and provisions:

	<u>2 0 1 6</u>	<u>2 0 1 5</u>
Payables for cash collateral received	\$ 1,126	\$ 5
Other liabilities	782	584
Taxes on earnings payable	336	364
Employee profit sharing payable	271	257
Clearing accounts	88	410
Provisions for other items	80	100
Security deposits	3	3
Total	<u>\$ 2,686</u>	<u>\$ 1,723</u>

NOTE 21. DIRECT LONG-TERM EMPLOYEE BENEFITS**a) Defined Contribution Retirement Plan -**

Beginning, 2006, the Institution modified the General Work Conditions (GWC) based on the trends and best practices with respect to managing and operating retirement schemes and pensions, in order to incorporate new employees, as well as those who decided to migrate from defined benefits system to defined contribution system. This scheme allows for having greater control over costs and liabilities of the plan, maintain an adequate cost-benefit ratio for the Institution and for workers, and it establishes clear contribution or retirement rules.

This plan consists of the contributions made by the Institution to open individual accounts in the name of each worker, which are divided into two subsidiary accounts denominated "A" and "B", respectively. It further consists of contributions made by the worker to subsidiary account "B" and on the yields generated by both subsidiary accounts, which are jointly identified as the worker's individual account.

The amount of contributions of the period allocated to income amounted to \$32 and \$27, respectively, at December 31, 2016 and 2015.

As of December 31, 2016 and 2015, the Defined Contribution Plan assets amount to \$269 and \$237, respectively, and it is invested in an irrevocable trust created in the Institution.

b) Defined Benefit Retirement Plan -

Moreover, GWCs set forth that workers who reach 65 years of age and complete 30 years of service will be eligible for a retirement annuity. Moreover, upon reaching 65 years of age with 5 years of seniority, workers will be eligible to receive a monthly annuity, whose amount will be equal to the result of multiplying the average of the net monthly salary accrued by the employee during the last year of service by the number of years of service rendered by the 0.0385 factor. The Institution reserves the right to pay a pension for retirement to that worker who has reached 60 years of age or completed 26 years of service.

On the other hand, the transition articles of the GWC dated August 12, 1994 set forth that workers who joined the Institution prior to the above date and reach 55 years of age and have completed 30 years of service, 60 years of age and have completed 26 years of service or 60 years of age and completed 5 years of seniority will be eligible for a pension in the terms of the GWC referred to above.

In the event of an unjustified dismissal or termination of the employer-employee relationship, the worker may choose to receive the pertinent indemnification or a retirement annuity calculated based on the main characteristics of the retirement plan discussed paragraph one if the worker is 50 years old and has 16 or more years of seniority.

Transition Article Five paragraph a) of the GWC, 2006 review, sets forth that persons who have obtained a pension for disablement, disability or retirement at a date prior to that review and those workers who have joined the Institution at a date prior to the effectiveness of the above review to whom the Defined Retirement Benefit Plan applies will continue to enjoy the right to receive the following additional benefits from the Institution at the time when they retire:

- Short-term loans, medium-term loans, and Special Loan for Savings, which will be paid with a charge to administration and promotion expenses with an 18% net guaranteed return of the maximum capacity to invest that will be calculated on 41.66% of the net monthly pension multiplied by 72 months, as well as the available capacity that will be over 50% of the net pension, less the month deductions from the short and medium-term loans with capital and interest multiplied by 72 months, with a 41.66% cap or ceiling of the monthly net pension. The Special Loan for Savings will bear 1% annual interest on its amount, which will be withheld by the Institution.

The net cost for the period allocated to income at December 31, 2016 and 2015 amounted to \$901 and \$1,041, respectively, including the effect of other postretirement benefits.

At December 31, 2016 and 2015, the plan assets of the fund for labor obligations amount to \$6,511 and \$6,429, respectively, and the fund is invested in an irrevocable trust created in the Institution. The net cost for the period recorded in income of the Institution amounted to \$298 and \$186, respectively.

In accordance with the provisions of FRS D-3 "Employee Benefits" (FRS D-3), the Institution recognized plan assets with respect to "other postretirement benefits" in its financial statements at December 31, 2016 and 2015, in the amounts of \$9,941 and \$9,502, respectively. Moreover, the net cost of the period recorded in income of the Institution amounted to \$603 and \$855, respectively.

The summary of the actuarial calculations at December 31, 2016 is as follows:

Item	Retirement	Seniority premium	Other benefits at retirement	Special Loan for Savings (PEA) and Financial Cost of Credits
	Retirement	Retirement and termination	Retirement	Retirement
Journal voucher for the recognition of losses and gains				
General description of benefits		Deferred amortization		
		In accordance with general labor conditions		
Vested Benefit Obligation	\$ 7,378	\$ 5	\$ 7,586	\$ 2,979

Reconciliation between the value of the Defined Benefit Obligation (DBO) and Plan assets (PA) with the net (Liability) / Asset for defined benefits (a)

A. Defined Benefit Obligations (DBO)	\$ (7,920)	\$ (28)	\$ (9,546)	\$ (3,654)
B. Plan Assets (PA)	6,571	29	6,977	3,104
Projected net (Liability) / Asset for defined benefits	\$ (1,349)	\$ 1	\$ (2,569)	\$ (550)
Amortization periods of unamortized items	6.30	11.20	15.38	6.30
Transition liability amortization period	N/A	N/A	N/A	N/A
Prior service amortization period	N/A	N/A	N/A	N/A

Net Cost for the Period 2016 (b)

A. Labor Cost	\$ 33	\$ 2	\$ 140	\$ 33
B. Financial Cost	458	2	531	231
C. Returns on Assets	(401)	(2)	(425)	(192)
D. Recycling of remeasurements	206	-	142	143
Net cost for the Period	\$ 296	\$ 2	\$ 388	\$ 215

Main hypothesis used:

	(a) 31-Dec-16	(b) 31-Dec-15
Discount rate	6.25%	6.25%
AP Rate of return	6.25%	6.25%
Rate of general wage increase	4.00%	4.00%
Rate of minimum wage increase	3.50%	3.50%
Medical inflation rate	9.00%	9.00%

- (a) Actuarial values were determined by the Bufete Matemático Actuarial, S.C. firm considered the hypotheses of December 31, 2016.
- (b) The hypotheses of December 31, 2015 were used to determine the net cost for the period of 2016.

The summary of the actuarial calculations at December 31, 2015 is as follows:

Item	Retirement	Seniority premium Retirement and termination	Other benefits at retirement	Special Loan for Savings (PEA) and Financial Cost of Credits
	Retirement	Retirement	Retirement	Retirement
Journal voucher for the recognition of losses and gains		Deferred amortization		
General description of benefits	In accordance with general labor conditions			
Vested Benefit Obligation	\$ <u>6,946</u>	\$ <u>6</u>	\$ <u>6,881</u>	\$ <u>3,118</u>

Reconciliation between the value of the Defined Benefit Obligation (DBO) and Plan assets (PA) with the Reserve or Project net Liability (PNP) at year end (a)

C. Defined Benefit Obligations (DBO)	\$ (7,577)	\$ (29)	\$ (8,655)	\$ (3,790)
D. Plan Assets (PA)	<u>6,375</u>	<u>26</u>	<u>6,572</u>	<u>2,940</u>
E. Funded Status	(1,202)	(3)	(2,083)	(850)
F. Actuarial (Gains) / losses	<u>1,258</u>	<u>4</u>	<u>2,071</u>	<u>872</u>
Net projected (Liability) / Asset at year end (PNP) (C+D)	\$ <u>56</u>	\$ <u>1</u>	\$ <u>(12)</u>	\$ <u>22</u>
Amortization periods of unamortized items	6.11	11.14	14.63	N/A
Transition liability amortization period	N/A	N/A	N/A	N/A
Prior service amortization period	N/A	N/A	N/A	N/A

Net Cost for the Period 2015 (b)

A. Labor Cost	\$ 30	\$ 1	\$ 187	\$ 28
B. Financial Cost	445	2	518	211
C. Returns on Assets	(395)	(1)	(383)	(181)
D. Amortization PPA	<u>104</u>	<u>-</u>	<u>449</u>	<u>26</u>
Net cost for the Period	\$ <u>184</u>	\$ <u>2</u>	\$ <u>771</u>	\$ <u>84</u>

Main hypothesis used:

	(c) 31-Dec-15	(d) 31-Dec-14
Discount rate	6.25%	6.25%
AP Rate of return	6.25%	6.25%
Rate of general wage increase	4.00%	4.00%
Rate of minimum wage increase	3.50%	3.50%
Medical inflation rate	9.00%	8.00%

(c) Actuarial values were determined by the Bufete Matemático Actuarial, S.C., which considered the hypotheses of December 31, 2015.

(d) The hypotheses of December 31, 2014 were used to determine the net cost for the period of 2015.

It is important to clarify that these results are not comparable with respect to the results generated and recorded in fiscal 2016, since the new provisions of the standard set forth treatments that differ from the prior standard applied to fiscal 2015, in results as well as in the application to stockholders' equity.

At those same dates, the general information of the pension and retirement plan is:

	2016	2015
Number of employees	1,056	1,017
Annual base payroll	\$ 276	\$ 257
Annual computed payroll	\$ 476	\$ 450
Average current age	42.40	43.46
Average seniority	12.00	12.94
Number of pensioners	1,555	1,526
Annualized pension payroll	\$ 506	\$ 483
Average current age	70.08	69.57

Statement of status

At December 31, 2016 and 2015, the statement of status is as follows:

	Retirement pension plan		Other benefits at retirement	
			Medical service, savings fund, insurance, athletic club	PEA and financial cost of credits
	Retirement	Seniority premium Retirement and termination	Retirement	Retirement
2016				
Defined benefit obligation	\$ (7,920)	\$ (28)	\$ (9,546)	\$ (3,654)
Plan assets	6,571	29	6,977	3,104
Defined benefits obligation in excess of the plan assets	(1,349)	1	(2,569)	(550)
Projected net (Liability) / Asset	\$ (1,349)	\$ 1	\$ (2,569)	\$ (550)
2015				
Defined benefit obligation	\$ (7,577)	\$ (29)	\$ (8,655)	\$ (3,790)
Plan assets	6,375	26	6,572	2,940
Defined benefits obligation in excess of the plan assets	(1,202)	(3)	(2,083)	(850)
Actuarial (gain) / loss carryforward	1,258	4	2,071	872
Projected net (Liability) / Asset	\$ 56	\$ 1	\$ (12)	\$ 22

Reconciliation of the book provision

At those same dates, the reconciliation of the book provision is as follows:

	Retirement pension plan		Other benefits at retirement	
			Medical service, savings fund, insurance, athletic club	PEA and financial cost of credits
	Retirement	Seniority premium Retirement and termination	Retirement	Retirement
2016				
Balance at beginning of year	\$ (56)	\$ (1)	\$ 12	\$ (22)
Remediations not yet recognized in OCI	1,259	4	2,070	872
Net cost for the period in accordance with FRS D-3	296	2	388	215
Contribution made to the fund	(296)	(2)	(388)	(215)
Recycling of remediations for defined benefits	146	(4)	487	(300)
Final balance	\$ 1,349	\$ (1)	\$ 2,569	\$ 550

	Retirement pension plan		Other benefits at retirement	
	Retirement	Seniority premium Retirement and termination	Medical service, savings fund, insurance, athletic club	PEA and financial cost of credits
2015				
Balance at beginning of year	\$ (56)	\$ -	\$ 12	\$ (22)
Net cost for the period in accordance with FRS D-3	184	1	1	84
Contribution made to the fund	(184)	(2)	(1)	(84)
Final balance	\$ (56)	\$ (1)	\$ 12	\$ (22)

In conformity with the provisions in the modifications of the Provisions published in the Official Daily Gazette (DOF) on December 31, 2015, and with the effectiveness of the new FRS D-3 issued by the CINIF, the Institution selected the progressive application referred to in temporary statute three of the above Provisions.

Pursuant to the foregoing, the balances indicated in paragraphs a) and b) of paragraph 81.2 of FRS D-3, balance of plan amendments not yet recognized and the accrued balance of plan gains and losses not recognized, respectively, will be recognized no later than fiscal 2021, by recognizing 20% beginning with its opening application, and an additional 20% in each one of the subsequent years until reaching 100% in a maximum period of 5 years.

The Commission was advised by the Institution of its decision to select the progressive application of the recognition of those balances on a timely basis.

The balance of plan amendments not yet recognized and accumulated balance of losses on the plan not yet recognized present an amount of \$(0.085) and \$(3,715), respectively. The initial effects that the application of FRS D-3 will have beginning the year in which its application starts is shown below:

- 1) The total balance of plan amendments not yet recognized amounting to \$(0.085), which will be recorded against prior year income.
- 2) 20% of the accumulated balance of plan losses amounting to \$(743) will be recorded in capital gains in the account of "Remeasurements of defined employee benefits". The remaining balance amounting to \$(2,972) will be applied in subsequent fiscal years over a maximum period of 5 years.

NOTE 22. INCOME TAX

The Institution is subject to the Income Tax regime in 2016 and 2015.

Income tax is calculated at a 30% rate considering certain impacts of inflation as taxable or deductible, such as depreciation calculated on constant values in constant pesos. The impact of inflation on certain monetary assets and liabilities is accumulated or deducted through the adjustment on inflation.

The provision in Income Tax is summarized as follows:

	<u>2016</u>	<u>2015</u>
Current	\$ <u>(824)</u>	\$ <u>(716)</u>
Deferred	\$ <u>279</u>	\$ <u>324</u>

Only deferred Income Tax and Employee Profit Sharing are calculated.

The main items included in the deferred tax accounts of the Institution and its subsidiaries are as follows:

	<u>2016</u>	<u>2015</u>
Liabilities:		
Investments in nondeductible fixed assets	\$ 279	\$ 296
Other assets	<u>627</u>	<u>406</u>
	\$ <u>906</u>	\$ <u>702</u>
Assets:		
Provisions	\$ (74)	\$ -
Valuation of permanent investments	-	(90)
Others	<u>(1,304)</u>	<u>(950)</u>
	<u>(1,378)</u>	<u>(1,040)</u>
Taxes on earnings	(472)	(338)
Deferred Employee Profit Sharing	<u>(303)</u>	<u>(203)</u>
Deferred taxes (net)	\$ <u>(775)</u>	\$ <u>(541)</u>

In 2016 and 2015, the effective rates stated as a percentage of income before taxes on earnings are:

	<u>2016</u>	<u>2015</u>
Statutory rate	30.00%	30.00%
Add (less):		
Nondeductible expenses	1.38%	2.44%
Portfolio provisions	18.30%	17.09%
Profit Sharing	(1.16%)	(1.14%)
Impact of inflation	(10.12%)	(6.55%)
Deferred tax	(14.72%)	(19.15%)
Others	5.08%	0.07%
Effective rate	<u>28.76%</u>	<u>22.76%</u>

NOTE 23. STOCKHOLDERS' EQUITY**a) Capital stock. -**

At December 31, 2016 and 2015, the Institution's capital stock is summarized as follows:

	<u>2 0 1 6</u>	<u>2 0 1 5</u>
Subscribed capital:		
<i>Series "A"</i>		
31 548 000 Certificates of Capital Contribution (CAPs) with a value amounting to fifty pesos each one	\$ 1,577	\$ 1,577
<i>Series "B"</i>		
16 252 000 CAPs with a value amounting to fifty pesos each one	813	813
Total subscribed for capital	<u>2,390</u>	<u>2,390</u>
Unissued capital		
<i>Series "A"</i>		
7 868 728 CAPs with a value amounting to fifty pesos each one	(393)	(393)
<i>Series "B"</i>		
4 053 586 CAPs with a value amounting to fifty pesos each one	(203)	(203)
Total unissued capital	<u>(596)</u>	<u>(596)</u>
Subscribed for and paid-in capital stock		
<i>Series "A"</i>		
23 679 272 CAPs with a value amounting to fifty pesos each one	1,184	1,184
<i>Series "B"</i>		
12 198 414 CAPs with a value amounting to fifty pesos each one	610	610
Total subscribed for and paid-in capital stock	<u>1,794</u>	<u>1,794</u>
Increase from restatement	7,011	7,011
Total	<u>\$ 8,805</u>	<u>\$ 8,805</u>

Series "A" represents 66% of the institution's capital, which may only be subscribed for by the Federal Government and Series "B" for the remaining 34%.

b) Contribution for future capital stock increases. -

At, December 31, 2016 and 2015, its value amounts to \$2,750 and \$1,950, respectively.

At its extraordinary meeting held on December 15, 2016, the Board of Directors authorized Management of the Institution, to carry out the necessary arrangements to petition the Executive

Branch, through the Ministry of Finance and Public Credit (SHCP), in an amount up to \$800 required to be able to support the volume of development and investment banking operations, as well as to obtain a prudential level of capitalization for fiscal 2016 year end. The above contribution was received and recorded in December 2016.

c) Paid stock premium. -

This premium applies to payments made by holders of Series "B" CAPs. The balance of the premiums paid at December 31, 2016 and 2015 amounts to \$8,922.

d) Capital reserves. -

The nominal value of these reserves at December 31, 2016 and 2015 amounts to \$314, and its restated value at both years end amounts to \$1,730.

e) Prior year losses. -

As of December 31, 2016 and 2015, the summary of the account balance is as follows:

	<u>2 0 1 6</u>	<u>2 0 1 5</u>
Gain or loss on the adjustment of changes in accounting policies by the Commission in Circular 1343.	\$ (2,860)	\$ (2,860)
Prior year income / loss	7,273	5,989
Creation of provisions for repossessed assets	(260)	(260)
RETANM realized	(13)	(13)
Pension reserve, PEA, and retiree loans.	<u>(4,310)</u>	<u>(4,310)</u>
	(170)	(1,454)
Gain or loss on valuation in associated and affiliated companies	3,319	3,319
Adjustment on accumulated depreciation of furniture and equipment	(96)	(96)
Deferred taxes	<u>(333)</u>	<u>(333)</u>
	<u>\$ 2,720</u>	<u>\$ 1,436</u>

f) Gain or loss on valuation of available-for-sale securities. -

The adjustments derived from valuations at market of available-for-sale securities are recorded in this line item. The gain or loss is recorded as realized in income up to the fiscal year in which the security is sold or reaches maturity.

At December 31, 2016 and 2015, the gain or loss on valuation of available-for-sale securities at market is summarized as follows:

	<u>2016</u>	<u>2015</u>
Valuation of available-for-sale securities	\$ <u>(178)</u>	\$ <u>(290)</u>

g) Effects of valuation of associated and affiliated companies. -

At, December 31, 2016 and 2015, its value amounts to \$640 and \$289, respectively.

h) Legal provisions. -

On November 23, 2008, the SHCP published rules for the capitalization requirements of Full-Service Banking Institutions and National Lending Institutions, Development Banking Institutions, which went into effect beginning January 1, 2010. These capitalization rules set forth the requirements with specific levels of net capital, as a percentage of both market and credit risk assets. In this particular respect, there is a 13.26% level confirmed by the Bank of Mexico at December 31, 2016.

Cash dividends received by legal entities resident in national territory are not subject to a withholding, unless they are drawn on items other than the Net Taxable Income Account (CUFIN-Spanish acronym).

NOTE 24. MAIN ITEMS THAT COMPRISE THE STATEMENT OF INCOME

The main items that comprise the Institution's Income (loss) at December 31, 2016 and 2015 are as follows:

	<u>2016</u>		
	<u>Total</u>	<u>Local currency</u>	<u>Foreign currency</u>
Interest income			
Interest on performing loan portfolio			
Commercial credits	\$ 2,114	\$ 898	\$ 1,216
Housing lending	2	2	-
Loans to government entities	716	715	1
Loans granted as a (Financial) Agent of the Federal Government	3	-	3
Loans to financial entities	6,014	5,738	276
	<u>\$ 8,849</u>	<u>\$ 7,353</u>	<u>\$ 1,496</u>
Interest and yields earned on investments in securities			
Trading securities	\$ 714	\$ 714	\$ -
Available-for-sale securities	278	-	278
Held-to-maturity securities	733	684	49
	<u>\$ 1,725</u>	<u>\$ 1,398</u>	<u>\$ 327</u>

	2 0 1 6		
	Total	Local currency	Foreign currency
Interest and yields earned in repurchase agreement transactions			
Repurchase transactions	\$ 10,097	\$ 10,097	\$ -
	<u>\$ 10,097</u>	<u>\$ 10,097</u>	<u>\$ -</u>
Interest from liquid assets			
Banks	\$ 46	\$ -	\$ 46
Restricted liquid assets	656	637	19
	<u>\$ 702</u>	<u>\$ 637</u>	<u>\$ 65</u>
Fees income from lending transactions (adjustment on yield)			
Commercial credits	\$ 94	\$ 94	\$ -
Revenues from hedge trading	(425)	(166)	(259)
Premiums on debt placement	13	13	-
Exchange gain on appreciation	108	-	108
Net equity dividends	4	4	-
Subsidiaries	20	20	-
Total interest income	<u>\$ 21,187</u>	<u>\$ 19,450</u>	<u>\$ 1,737</u>
Interest expenses			
Interest on term deposits	\$ 5,430	\$ 5,266	\$ 164
Interest on negotiable instruments issued	3,214	2,687	527
Interest payable on interbank loans and loans for other Agencies	469	235	234
Interest and yields payable in repurchase agreement transactions	9,057	9,057	-
Expenses from hedge trading	(1,277)	(2,863)	1,586
Subsidiaries	(443)	(443)	-
Total interest expense	<u>\$ 16,450</u>	<u>\$ 13,939</u>	<u>\$ 2,511</u>
Financial margin	<u>\$ 4,737</u>	<u>\$ 5,511</u>	<u>\$ (774)</u>
Commission and fee income			
Guarantees	\$ 1,931	\$ 1,931	\$ -
Lending transactions	195	195	-
Guarantees by endorsement	2	2	-
Custody or administration of assets	8	8	-
Fiduciary activities	334	334	-
Others	74	3	71
Subsidiaries	227	227	-
	<u>\$ 2,771</u>	<u>\$ 2,700</u>	<u>\$ 71</u>

	2016		
	Total	Local currency	Foreign currency
Commission and fee expenses			
Loans received	\$ 24	\$ -	\$ 24
Debt placed	9	9	-
Others	91	85	6
Subsidiaries	165	165	-
	<u>\$ 289</u>	<u>\$ 259</u>	<u>\$ 30</u>
Gain or loss on brokerage			
Gain or loss on valuation at fair value and decrease on securities valued at cost:			
Trading securities	\$ 186	\$ 186	\$ -
Derivative financial instruments for trading purposes	140	(73)	213
Derivative financial instruments for hedging purposes	(15)	1,694	(1,709)
Collateral sold	(301)	(301)	-
	<u>\$ 10</u>	<u>\$ 1,506</u>	<u>\$ (1,496)</u>
Gain or loss on trading derivative financial instruments:			
Trading securities	\$ 565	\$ 565	\$ -
Held-to-maturity securities	2	-	2
Available-for-sale securities	(26)	-	(26)
Derivatives financial instruments for trading purposes	3,804	3,804	-
	<u>\$ 4,345</u>	<u>\$ 4,369</u>	<u>\$ (24)</u>
Gain (loss) on buying and selling foreign currency	\$ (5,101)	\$ -	\$ (5,101)
Gain or loss on brokerage	<u>\$ (746)</u>	<u>\$ 5,875</u>	<u>\$ (6,621)</u>
Other operating income (expenses)			
Reversal of the surplus of preventive estimates for lending risks	\$ 579	\$ 426	\$ 153
Allowance for uncollectible or doubtful accounts	(15)	(15)	-
Allowance (provision) for loss on repossessed assets	(3)	(3)	-
Other losses	(7)	(7)	-
Gain or loss on sale of repossessed assets	2	2	-
Income on loans to personnel	40	40	-
Other operating income (expenses) items (a)	(435)	(435)	-
Other income (expenses) of subsidiaries	(20)	(20)	-
	<u>\$ 141</u>	<u>\$ (12)</u>	<u>\$ 153</u>

- (a) The Institution realized the payment in the amount of \$800 million Mexican pesos on December 9, 2016, in conformity with the indications in official letter number 102-B-023, dated December 8, 2016, issued by the Vice Ministry of Finance and Public Credit, whereby the Federal Government instructs the Institution to realize a payment under the juridical nature of use for furnishing a sovereign guarantee of the Federal Government.

	2 0 1 5		
	Total	Local currency	Foreign currency
Interest income			
Interest on performing loan portfolio			
Commercial credits	\$ 1,454	\$ 888	\$ 566
Housing lending	1	1	-
Loans to government entities	392	391	1
Loans granted as a (Financial) Agent of the Federal Government	12	-	12
Loans to financial entities	4,267	4,010	257
	<u>\$ 6,126</u>	<u>\$ 5,290</u>	<u>\$ 836</u>
Interest and yields earned on investments in securities			
Trading securities	\$ 195	\$ 195	\$ -
Available-for-sale securities	228	-	228
Held-to-maturity securities	592	544	48
	<u>\$ 1,015</u>	<u>\$ 739</u>	<u>\$ 276</u>
Interest and yields earned in repurchase agreement transactions			
Repurchase transactions	\$ 7,880	\$ 7,880	\$ -
	<u>\$ 7,880</u>	<u>\$ 7,880</u>	<u>\$ -</u>
Interest from liquid assets			
Banks	\$ 7	-	\$ 7
Restricted liquid assets	443	435	8
	<u>\$ 450</u>	<u>\$ 435</u>	<u>\$ 15</u>
Fees income from lending transactions (adjustment on yield)			
Commercial credits	\$ 94	\$ 93	\$ 1
Revenues from hedge trading	\$ (1,243)	\$ (1,340)	\$ 97
Net equity dividends	\$ 2	\$ 2	\$ -
Subsidiaries	\$ 92	\$ 92	\$ -
Total interest income	<u>\$ 14,416</u>	<u>\$ 13,191</u>	<u>\$ 1,225</u>
Interest expenses			
Interest on term deposits	\$ 3,291	\$ 3,230	\$ 61
Interest on negotiable instruments issued	2,104	1,960	144
Interest payable on interbank loans and loans for other Agencies	209	70	139
Interest and yields payable in repurchase agreement transactions	6,328	6,328	-
Expenses from hedge trading	(1,960)	(1,989)	29
	<u>\$ 9,972</u>	<u>\$ 9,599</u>	<u>\$ 373</u>
Exchange loss on appreciation	129	-	129
Total interest expense	<u>\$ 10,101</u>	<u>\$ 9,599</u>	<u>\$ 502</u>
Financial margin	<u>\$ 4,315</u>	<u>\$ 3,592</u>	<u>\$ 723</u>

	2015		
	Total	Local currency	Foreign currency
Commission and fee income			
Guarantees	\$ 1,811	\$ 1,811	\$ -
Lending transactions	207	207	-
Guarantees by endorsement	2	2	-
Custody or administration of assets	8	8	-
Fiduciary activities	307	307	-
Others	22	2	20
Subsidiaries	305	305	-
	<u>\$ 2,662</u>	<u>\$ 2,642</u>	<u>\$ 20</u>
Commission and fee expenses			
Loans received	\$ 10	\$ -	\$ 10
Debt placed	7	5	2
Others	76	68	8
Subsidiaries	205	205	-
	<u>\$ 298</u>	<u>\$ 278</u>	<u>\$ 20</u>
Gain or loss on brokerage			
Gain or loss on valuation at fair value and decrease on securities valued at cost:			
Trading securities	\$ 314	\$ 314	\$ -
Derivative financial instruments for trading purposes	3	2	1
Derivative financial instruments for hedging purposes	(61)	69	(130)
	<u>\$ 256</u>	<u>\$ 385</u>	<u>\$ (129)</u>
Gain or loss on trading derivative financial instruments:			
Trading securities	\$ 109	\$ 109	\$ -
Available-for-sale	2	-	2
Derivative financial instruments for trading purposes	4,382	4,382	-
Gain on foreign currency trading	(5,162)	-	(5,162)
	<u>\$ (669)</u>	<u>\$ 4,491</u>	<u>\$ (5,160)</u>
Gain or loss on brokerage	<u>\$ (413)</u>	<u>\$ 4,876</u>	<u>\$ (5,289)</u>
Other operating income (expenses)			
Reversal of the surplus of preventive estimates for lending risks	\$ 546	\$ 316	\$ 230
Allowance (provision) for loss on repossessed assets	(7)	(7)	-
Other losses	(13)	(13)	-
Income on loans to personnel	39	39	-
Other operating income (expenses) items	(b) (534)	(536)	2
Other income (expenses) of subsidiaries	(13)	(13)	-
	<u>\$ 18</u>	<u>\$ (214)</u>	<u>\$ 232</u>

- (b) The Institution realized the payment in the amount of \$700 million Mexican pesos on December 9, 2015, in conformity with the indications in official letter number 102-B-077, dated December 8, 2015, issued by the Vice Ministry of Finance and Public Credit, whereby the Federal Government instructs the Institution to realize a payment under the juridical nature of use for furnishing a sovereign guarantee of the Federal Government.

NOTE 25. COMMITMENTS AND CONTINGENCIES

Guarantees by endorsement executed

At December 31, 2016 and 2015, the Institute has guarantees by endorsements furnished amounting to \$72 and \$109, respectively, which represent a contingent risk in the event that the secured debtor liquidates his debt to the lending institution. At December 31, 2016 and 2015, losses on guarantees have not been recorded in income of the Institution. However, in the event of nonperformance by any secured drawer, the Institution grants a credit to meet its obligation.

During 2016, no credits have been granted due to nonperformance.

Contingent assets and liabilities

At December 31, 2016 and 2015, this item for \$53,448 and \$49,738, respectively, is summarized as follows:

		<u>2016</u>	<u>2015</u>
Contingent liabilities:			
Guarantees furnished	(a) \$	63,537	\$ 59,541
Unreimbursed guaranties paid covered by a counter guaranty	(b)	11,715	12,041
Receivables on claims		134	135
Commitments acquired		<u>2,118</u>	<u>1,848</u>
		<u>77,504</u>	<u>73,565</u>
Contingent assets:			
Counter guaranty received from the Counter guaranty Trust for Enterprise Financing	(c)	11,645	11,181
Unrecovered guaranties paid covered by a counter guarantors	(d)	11,715	12,041
Unrecovered guaranties paid without a counter guaranty	(e)	<u>696</u>	<u>605</u>
		<u>24,056</u>	<u>23,827</u>
Total	\$	<u>53,448</u>	<u>\$ 49,738</u>

- (a) In the item of guarantees furnished, the institution has mainly guarantees furnished through the Fund for Risk Equity and the Fund for Surety Bond Equity Risk, both of which present guarantees furnished amounting to \$60,116 and \$57,574, respectively, at December 31, 2016 and 2015. The spread amounting to \$3,421 and \$1,967 at December 31, 2016 and 2015, respectively, correspond to selective guarantees granted directly by the Institution. These

guarantees represent the amount of liabilities assumed by the Institution for guaranteeing financial brokers the recovery of their loan portfolio.

- (b) The Institution's contingent obligation of reimbursing the amount of the guaranties paid mainly to the Counterguaranty Trust for Business Financing has been recognized in this item. Those paid guarantees did have the counterguaranty and continue to be in the process of being recovered by the bank and non-bank financial brokers.
- (c) The Fund for Risk Equity reduces the Institution's contingency through a counterguaranty received from the Counterguaranty Trust for Enterprise Financing, the promoter of granting credits for specific purposes, which has assigned funds for these purposes for \$11,645 and \$11,181, respectively, at December 31, 2016 and 2015. These funds assure the recovery up to these amounts of the guarantees exercised by financial brokers, who assume the commitment of negotiating the recovery of the credits of their final borrowers judicially and out-of-court.

In addition to that counterguaranty, the Fund has created a preventive estimate for credit risks for \$1,175 and \$705 at December 31, 2016 and 2015, respectively, in terms of the provisions set forth by the Commission.

Having received the counterguaranty, as well as the level of preventive estimate created, the Institution considers that exposure is covered and supports it in the experience observed in the guarantee program.

- (d) The contingent right that the institute has of recovering the amount of guarantees paid that had a counterguaranty that were mainly covered by the Counterguaranty Trust for Enterprise Financing has been recognized in this item, and continues in the recovery process by banking and non-banking financial brokers.
- (e) The item of unrecovered guarantees without a counterguaranty, the amount of guarantees honored by the institution have been recognized that are in the process of being recovered by financial brokers that was not covered by the Counterguaranty Trust for Enterprise Financing.

Credit commitments

At December 31, 2016 and 2015, the Institution has lines of credit and lines of guarantees furnished to financial brokers that have not been drawn down for \$135,025 and \$197,020, respectively. The amount of \$44,013 at December 31, 2016 applies to lines of credit and \$91,012 to lines of guarantees furnished, respectively, whereas at December 31, 2015, the amount of \$56,790 applies to lines of credit and \$140,230 to lines of guarantees furnished, respectively.

NOTE 26. ASSETS PLACED IN TRUST, MANDATE, AND FINANCIAL AGENT OF THE FEDERAL GOVERNMENT

At December 31, 2016 and 2015, the balances of transactions in which the Institution acts as a Trustee are summarized as follows:

	<u>2016</u>	<u>2015</u>
Investment trusts	\$ 25,967	\$ 24,081
Management trusts	1,093,806	1,034,677
Trust deeds	<u>46,685</u>	<u>50,078</u>
	1,166,458	1,108,836
Mandates	<u>13,716</u>	<u>2,657</u>
	1,180,174	1,111,493
Financial Agent of the Federal Government	<u>364,371</u>	<u>291,883</u>
Total	<u>\$ 1,544,545</u>	<u>\$ 1,403,376</u>

Investment and management trusts refer to entities with their own legal personality, independent from the institution. These balances represent the valuation of Trust Assets which, overall, represent assets valued with distinct accounting practices which essentially represent neither rights of the entity nor the contingency to which the Institution is subject in the event of nonperformance in its role as a trustee.

The deeds of trust apply to entities that maintain credits, securities, real properties, etc. as part of its assets held in trust that serve as a guarantee for the liquidation of financing received the trustors thereof from other lending institutions. The Institution only acts as a trustee in those entities.

The institution's revenues from Trustee Activities at December 31, 2016 and 2015 amounted to \$189 and \$188, respectively.

At December 31, 2016 and 2015, trust accounts include a balance amounting to \$449 and \$464, respectively, that apply to the patrimony of the Portfolio Recovery Trust (FIDERCA), which manages doubtful accounts that were originally the Institution's and were transferred to the Federal Government in the course of 1996. The Institution currently holds the respective beneficiary interests.

The Institution created the trust to strengthen its capital, in compliance with the provisions set forth in Article 55 Bis of the Lending Institutions Law, and in conformity with the general rules that both Domestic Lending Institutions and Development Banking Institutions should be subject to in order for them to operate, published in the Official Daily Gazette on October 24, 2002.

NOTE 27. CUSTODY AND ADMINISTRATION OF ASSETS

These mainly represent the control of contractual documentation that supports the securities trading and lending operations. Moreover, it includes the total securities issued by the Institution and managed for account of clients. At December 31, 2016 and 2015, they are summarized as follows:

	<u>2 0 1 6</u>	<u>2 0 1 5</u>
Custody	\$ 70,324	\$ 106,017
Pledged securities	235,720	181,069
Collections	1	1
Securities in administration	275,309	254,742
Subsidiaries	12,151	11,085
	<u>\$ 593,505</u>	<u>\$ 552,914</u>

The fees collected by the Institution for this type of activities at December 31, 2016 and 2015 amount to \$8 in both years.

NOTE 28. OTHER MEMORANDUM ACCOUNTS

At December 31, 2016 and 2015, the balances of other memorandum accounts are summarized as follows:

	<u>2 0 1 6</u>	<u>2 0 1 5</u>
Guarantees paid reported by brokers as uncollectible without a counterguaranty	(a) \$ 71	\$ 49
Classification by degree of loan portfolio risk	277,922	231,352
Credits obtained not yet drawn down (Note 19)	3,005	7,559
Other memorandum accounts	(b) 329,809	337,957
Total	<u>\$ 610,807</u>	<u>\$ 576,917</u>

- (a) They correspond to the amounts of unrecovered guarantees on which collection procedures have been exhausted by the brokers, which do not have a counterguaranty.
- (b) Other memorandum accounts are included for control of renewed and restructured credits, uncollectible credits, uncollectible credits applied against the provision, mortgage-backed credits, certificates and coupons to be incinerated, VAT recorded by states, portfolio recovery, issue of provisional certificates, repossessed assets or received as written-off payment preventively, control of amounts contracted in repurchase agreements and derivative instruments, commitments, preventive reserves of portfolio financial brokers, and various unspecified items

NOTE 29. SEGMENT INFORMATION

The factors used for identifying business segments considered the nature of the activities carried out, the existence of specific administrators for those activities, the generation of revenues and expenses thereof, as well as the follow-up regularly performed on the results generated that are presented regularly to the Board of Directors of the Institution.

The segment of markets and treasury includes investments carried out in money, capital, exchange and treasury markets.

The loan portfolio placed directly with the public sector and private sector is considered for the first tier credit segment, whereas the loan portfolio channeled through bank and non-bank financial brokers was considered for the second tier credit.

Guarantees furnished to banks and non-bank financial brokers are included in the segment of credit guarantees. The balances of this segment are presented in memorandum accounts that amount to \$59,594 and \$56,684 at December 31, 2016 and 2015, respectively.

The balances of the financial Agent segment apply to activities realized by Federal Government Law, in order to manage funds obtained from international financial agencies in its name. At December 31, 2016 and 2015, they present a balance amounting to \$364,465 and \$291,992, of which the amounts of \$364,371 and \$291,883 are recorded in memorandum accounts.

Proprietary and external trust management services are included in the Trustee segment, which are presented in memorandum accounts and amount to \$1,166,458 and \$1,111,493 at December 31, 2016 and 2015.

Everything relative to investment banking and balances of subsidiaries are included in the segment of other areas. As an investment bank, credit restructuring fees are handled for security market guarantees, as well as gains or losses on equity in risk capital of public and private companies.

At December 31, 2016 and 2015, assets and liabilities and net income of the main operations of the Institution's business segments are presented below:

Business segments	Assets		Liabilities and Capital		Net income (loss)	
	Amount	Equity	Amount	Equity	Amount	Equity
2016						
Markets and treasury	\$ 255,965	50.83%	\$ 255,965	50.83%	\$ 1,168	88.42%
First tier credit	66,299	13.17%	66,299	13.17%	(125)	-9.46%
Second tier credit	147,920	29.38%	147,920	29.38%	809	61.24%
Loan guarantees	-	-	-	-	842	63.74%
Financial broker	94	0.02%	94	0.02%	101	7.65%
Trustee	-	-	-	-	(8)	-0.61%
Other areas	33,263	6.60%	33,263	6.60%	270	20.44%
Use and expense of retirees	-	-	-	-	(1,736)	-131.42%
Total	\$ 503,541	100.00%	\$ 503,541	100.00%	\$ 1,321	100.00%

Business segments	Assets		Liabilities and Capital		Net income (loss)	
	Amount	Equity	Amount	Equity	Amount	Equity
2015						
Markets and treasury	\$ 201,534	52.39%	\$ 201,534	52.39%	\$ 1,099	85.59%
First tier credit	43,730	11.37%	43,730	11.37%	357	27.80%
Second tier credit	127,863	33.24%	127,863	33.24%	486	37.85%
Loan guarantees	-	-	-	-	665	51.79%
Financial broker	109	0.03%	109	0.03%	65	5.06%
Trustee	-	-	-	-	3	0.23%
Other areas	11,474	2.97%	11,474	2.97%	376	29.28%
Use and expense of retirees	-	-	-	-	(1,767)	-137.64%
Total	\$ 384,710	100.00%	\$ 384,710	100.00%	\$ 1,284	100.00%

Statements of income by business segments at December 31, 2016 and 2015 are presented below:

	Markets and treasury	First tier credit	Second tier credit	Loan guarantees	Financial broker	Trustee	(a) Other areas	Use and expense of retirees	Total
2016									
<i>Income:</i>									
Financial income, net	\$ 1,613	\$ 552	\$ 1,390	\$ 2,248	\$ 233	\$ 193	\$ 401	\$ -	\$ 6,630
<i>Expenses:</i>									
Operating expense	(350)	(72)	(640)	(332)	(121)	(188)	(109)	-	(1,812)
Operating income	1,263	480	750	1,916	112	5	292	-	4,818
Credit reserves and write-offs	(4)	(601)	115	(633)	(2)	(3)	(1)	-	(1,129)
Retiree expense	-	-	-	-	-	-	-	(936)	(936)
Other Expenses and Taxes	(b) (91)	(4)	(56)	(441)	(9)	(10)	(21)	(800)	(1,432)
Net income (loss)	\$ 1,168	\$ (125)	\$ 809	\$ 842	\$ 101	\$ (8)	\$ 270	\$ (1,736)	\$ 1,321
2015									
<i>Income:</i>									
Financial income, net	\$ 1,539	\$ 537	\$ 1,417	\$ 1,931	\$ 195	\$ 193	\$ 461	\$ -	\$ 6,273
<i>Expenses:</i>									
Operating expense	(360)	(67)	(701)	(309)	(121)	(177)	(59)	-	(1,794)
Operating income	1,179	470	716	1,622	74	16	402	-	4,479

	<u>Markets and treasury</u>	<u>First tier credit</u>	<u>Second tier credit</u>	<u>Loan guarantees</u>	<u>Financial broker</u>	<u>Trustee</u>	<u>(a) Other areas</u>	<u>Use and expense of retirees</u>	<u>Total</u>
Operating income	1,179	470	716	1,622	74	16	402	-	4,479
Credit reserves and write-offs	(2)	(90)	(179)	(642)	(1)	(1)	-	-	(915)
Retiree expense	-	-	-	-	-	-	-	(1,067)	(1,067)
Other Expenses and Taxes	(c) (78)	(23)	(51)	(315)	(8)	(12)	(26)	(700)	(1,213)
Net income (loss)	\$ 1,099	\$ 357	\$ 486	\$ 665	\$ 65	\$ 3	\$ 376	\$ (1,767)	\$ 1,284

(a) It includes the following areas: Investment Bank, Subsidiaries and Other Income (Expenses), net.

(b) It includes \$632 of taxes and Employee Statutory Profit Sharing due and deferred.

(c) It includes \$513 of taxes and Employee Statutory Profit Sharing due and deferred.

Retained earnings amounted to \$1,613 in 2016, which is mainly comprised of \$1,523 generated by the operation of distinct markets and treasury, which was higher for \$105 or 6.9%, in connection with what was obtained in 2015.

At December 31, 2016, net income obtained in the first tier Credit amounted to \$552, consisting of a financial margin of \$492; of extraordinary income of normal and default interest \$24, and net fees amounting to \$36, which include \$5 of fees identified with the previously referred to client, as well as the payment of \$10 on commitment fees associated with credits contracted with the IDB.

The second tier Credit obtained accrued financial income amounting to \$1,390, of which \$1,311 correspond to financial margin, and \$79 to commission fees, and other net income associated with the lending operation. The amount of financial margin was lower in 2016 compared with that observed in 2015, due to the reduction of 23 base points in the weighted margin of the loan portfolio. That reduction of financial margin concurred with the behavior of market rates, as well as the institutional strategy of offering more competitive rates to brokers. Moreover, the average balance between both periods increased 18.6% by going from \$102,951 in 2015 up to \$122,080 in 2016, in line with institutional strategy.

At December 31, 2016, the credit Guarantee segment presents net financial income amounting to \$2,249, which includes fees collected on guarantees furnished amounting to \$1,796, as well as \$453 of interest on investments and net recoveries.

Net financial income of the credit Guarantee segment increased 16.4% from 2015 to 2016, mainly due to the growth in the balance of proprietary guarantees furnished during the last twelve months, which went from \$59,541 up to \$63,536, equivalent to 6.7%.

At December 31, 2016, net financial income of the Financial Agent segment amounted to \$233. With respect to what was obtained due partly to the variation in the exchange rate in 2015, these fees are collected in dollars, and at the increase in the balance of the 4.4% mandate in dollars.

Net financial income was charged for \$193 in the Trustee business segment in 2016. It is practically the same amount as in the prior year, in spite of the payment of \$4 for consulting for reorganization of this business area, which represented a 2% increase without considering the above expense.

NOTE 30. COMPREHENSIVE INCOME

The Institution's comprehensive income for the years ended December 31, 2016 and 2015 is presented below:

	<u>2016</u>	<u>2015</u>
Net income for the year	\$ 1,321	\$ 1,284
Effect of items recognized in stockholders equity with no effect in results of the year:		
Gain (loss) on valuation of available-for-sale securities	112	(238)
Valuation effects in associate and affiliate companies	351	126
Non-holding company equity	139	118
	<u>602</u>	<u>6</u>
Comprehensive income or loss	\$ <u>1,923</u>	\$ <u>1,290</u>

NOTE 31. CAPITALIZATION RATIO

At December 31, 2016 and 2015, the preliminary of the capitalization ratio was set at 13.26% and 13.57%, which is comprised of and starts with net capital amounting to \$22,657 and assets adjusted for total risks amounting to \$170,817.

a) *Basic and Complementary Capital.*

The Institution's net capital consists of \$22,657 of basic capital. Pursuant to the application of the portfolio rating methodology, complementary capital is zero, which implies that Net Capital is equal to Basic Capital that is, in turn, equal to Basic Capital.

b) *Assets adjusted for market risks.*

Assets adjusted for market risks amount to \$47,849 and are equivalent to a capital requirement amounting to \$3,828, which are summarized as follows:

Positions exposed to market risk by the risk factor

Item	Amount of equivalent positions	Capital requirement
Transactions in local currency at a nominal rate	\$ 12,196	\$ 975
Trades with debt securities in local currency with a surcharge and a reviewable rate	6,714	540
Transactions in local currency at a real rate or denominated in UDIS	15,036	1,202
Positions in UDIS or with a return based on the NCPI	62	5
Transactions in foreign currency at a nominal rate	3,646	291
Foreign exchange positions or with a yield indexed to the exchange rate	138	11
Positions in shares with a return indexed to the price of a share of group of shares	10,057	804
	\$ 47,849	\$ 3,828

c) Assets adjusted for credit risks.

Assets adjusted for credit risks amount to \$115,623 and are equivalent to a capital requirement amounting to \$9,250. Pursuant to the foregoing, the assets adjusted for credit risks in credits and deposits amount to \$87,246, which are equivalent to a capital requirement amounting to \$6,980, which are summarized as follows:

Weighted assets subject to credit risk by risk group

Item	Assets Weighted by Risk	Capital requirement
Group III (weighted at 20%)	\$ 13,936	\$ 1,115
Group III (weighted at 50%)	2,454	196
Group III (weighted at 100%)	872	70
Group III (weighted at 120%)	536	43
Group IV (weighted at 20%)	3,514	281
Group VI (weighted at 100%)	685	55
Group VII (weighted at 20%)	6,646	532
Group VII (weighted at 50%)	3,511	281
Group VII (weighted at 100%)	12,916	1,033
Group VII (weighted at 120%)	9	1
Group VII (weighted at 150%)	3,994	319
Group VII-B (weighted at 20%)	81	7
Group VII-B (weighted at 50%)	913	73
Group VII-B (weighted at 100%)	37,060	2,965
Group VIII (weighted at Group VI%)	5	-
Group VIII (weighted at Group VII%)	114	9
	\$ 87,246	\$ 6,980

d) **Assets adjusted for operating risks.**

Assets adjusted for operating risks amount to \$7,345 and are equivalent to a capital requirement amounting to \$588.

Weighted assets subject to operating risk

Method used	Assets weighted by risk	Capital requirement
Basic indicator	\$7,345	\$588
Average market and credit risk requirement of the last 36 months	\$10,654	Average positive annual net revenue of the last 36 months \$3,917

Annex 1-O of the Provisions, requirements for the disclosure of information relative to capitalization

1. Summary of net capital.

Ref.	Common capital tier 1 (CET 1) Instruments and reserves	Amount
1	Common shares that qualify for level 1 common capital plus its applicable premium	\$ 20,477
2	Prior year losses	2,720
3	Other elements of comprehensive capital (and other reserve)	2,873
6	Common tier 1 capital before regulatory adjustments	\$ 26,070
	Common tier 1 capital: regulatory adjustments	
15	Defined benefit pension plan	13,405
26	Domestic regulatory adjustments	3,413
A	of which: Other elements of comprehensive capital (and other reserve)	
D	of which: Investments in multi-lateral agencies	673
F	of which: Investments in risk capital	2,576
G	of which: Investments in mutual funds	164
28	Total regulatory adjustments to tier 1 common capital	\$ 3,413
29	Common capital tier 1 (CET 1)	\$ 22,657
	Additional tier 1 capital: regulatory adjustments	
44	Additional tier 1 capital (AT1)	\$ -
45	Tier 1 capital (T1 = CET1 + AT1)	\$ 22,657
	Tier 2 capital: instruments and reserves	
51	Tier 2 capital before regulatory adjustments	-

Ref.	Common capital tier 1 (CET 1) Instruments and reserves	Amount
	Tier 2 capital: regulatory adjustments	-
59	Total capital (TC = T1 + T2)	\$ 22,657
60	Assets weighted by total risks	\$ 170,817
	Capital ratios and supplements	
61	Common tier 1 capital (as a percentage of the weighted assets by total risks)	13.26%
62	Tier 1 capital (as a percentage of the weighted assets by total risks)	13.26%
63	Total Capital (as a percentage of the weighted assets by total risks)	13.26%
64	Specifically institutional supplement (it should at least consist of the common tier 1 capital requirement, plus the capital conservation buffer, plus the countercyclical buffer, plus the G-SIB buffer stated as a percentage of the total weighted risk assets).	7.00%
65	of which: Conservation capital supplement	2.50%
68	Tier 1 common capital available to cover supplements (as a percentage of the total weighted risk assets)	6.26%

2. Ratio of net capital with the balance sheet

Balance sheet amounts		
Reference of the items of the balance sheet	Items of the balance sheet (unconsolidated)	2016
	Assets:	
BG1	Liquid assets	\$ 15,697
BG2	Memorandum accounts	-
BG3	Investments in securities	240,002
BG4	Receivables under repurchase agreements	20
BG5	Securities lending	-
BG6	Derivatives	182
BG7	Valuation adjustment on hedges of financial assets	71
BG8	Total loan portfolio (net)	209,849
BG9	Benefits receivable on securities trading	-
BG10	Other receivables (net)	25,639
BG11	Repossessed assets (net)	9
BG12	Property, furniture and equipment (net)	7
BG13	Permanent investments	(a) 21,185
BG14	Long-lived assets held for sale	-
BG15	Deferred taxes and employee profit sharing (net)	1,294
BG16	Other assets	1,120
	Total assets	\$ 515,075

Balance sheet amounts

Reference of the items of the balance sheet	Items of the balance sheet (unconsolidated)	2 0 1 6
Liabilities:		
BG17	Traditional deposits	\$ 245,276
BG18	Interbank loans and from other agencies	30,350
BG19	Payables under repurchase agreements	202,689
BG20	Securities lending	-
BG21	Collateral sold or furnished as a guarantee	-
BG22	Derivatives	9,555
BG23	Valuation adjustment on hedges of financial liabilities	(3,699)
BG24	Debentures in securities trading	-
BG25	Other payables	4,154
BG26	Outstanding unsecured obligations	-
BG27	Deferred taxes and employee profit sharing (net)	-
BG28	Deferred credits and advance payments from customers	40
	Total liabilities	<u>488,365</u>
Stockholders' equity:		
BG29	Capital contributions	20,477
BG30	Capital gains	6,233
	Total stockholders' equity	<u>26,710</u>
	Total liabilities and stockholders' equity	<u>\$ 515,075</u>
Memorandum accounts:		
BG31	Guarantees by endorsement executed	\$ 72
BG32	Contingent assets and liabilities	\$ 68,803
BG33	Credit commitments	\$ 44,012
BG34	Assets placed in trust or legal custody	\$ 1,180,174
BG35	Financial agent of the Federal Government	\$ 364,371
BG36	Assets in custody or administration	\$ 581,354
BG37	Collateral received by the entity	\$ 22,298
BG38	Collateral received and sold or furnished as a guarantee by the entity	\$ 22,277
BG39	Investment bank third party trading (net)	\$ 77,010
BG40	Uncollected accrued interest derived from the nonperforming portfolio	\$ 190
BG41	Other memorandum accounts	\$ 603,737

(a) Other investments included

3. Main characteristics of the securities that form part of net capital (Series A)

Ref.	Characteristic	Options
1	Issuer	Nacional Financiera, Sociedad Nacional de Crédito
2	identifier ISIN, CUSIP o Bloomberg	In conformity with Article 30 of the Lending Institutions Act, Nacional Financiera, National Lending company, Development Banking Institution is governed by its Internal Regulations, holders of Series "A" certificates of capital contribution, if applicable, will have the rights set forth in Article 35 of the Lending Institutions Act and Article 12 of the Internal Regulations of Nacional Financiera.
3	Legal framework	
Regulatory treatment		
4	Capital level with transitory status	Basic 1 Lending institution without consolidating subsidiaries
5	Capital level without transitory status	
6	Level of instrument	
7	Type of instrument	Series "A" certificate of capital contribution
8	Amount recognized in regulatory capital	66% in accordance with (3)
9	Nominal value of the instrument	50.00
9A	Currency of the instrument	Mexican pesos
10	Book classification	Capital
11	Issue date	Perpetuity Without maturity
12	Term of the instrument	
13	Expiration date	
14	Prepaid expense clause	No
15	First prepaid expense date	
15A	Regulatory or tax events	
15B	Liquidation prices of prepaid expense clause	
16	Subsequent prepaid expense dates	
Yields / dividends		
17	Type of yield / dividend	Variable
18	Interest rate / dividend	Variable
19	Dividend cancellation clause	No
20	Discretionary nature in the payment	Completely discretionary
21	Interest increase clause	No
22	Yield / dividend	Noncumulative
23	Convertibility of the instrument	Nonconvertible
24	Convertibility conditions	
25	Degree of convertibility	
26	Conversion rate	
27	Type of instrument convertibility	

Ref.	Characteristic	Options
28	Type of financial instrument of convertibility	
29	Issuer of instrument	
30	Write - down clause	
31	Write - down conditions	
32	Degree of write - down	
33	Temporary status of write - down	
34	Temporary value write - down mechanism	
35	Subordinated position in case of liquidation	
36	Nonperformance characteristics	
37	Description of nonperformance characteristics	

Risk Management Policies

The institutional **strategy** is derived from the mission and business strategy. Risk strategy is developed by considering target profitability, as well as the desired risk profile, based on institutional strategy.

The risk management **process** consists of identification, measurement, monitoring, control, limitation, and risk information. This process applies to all types of managed risk.

The interaction between strategy and risk process is presented below:

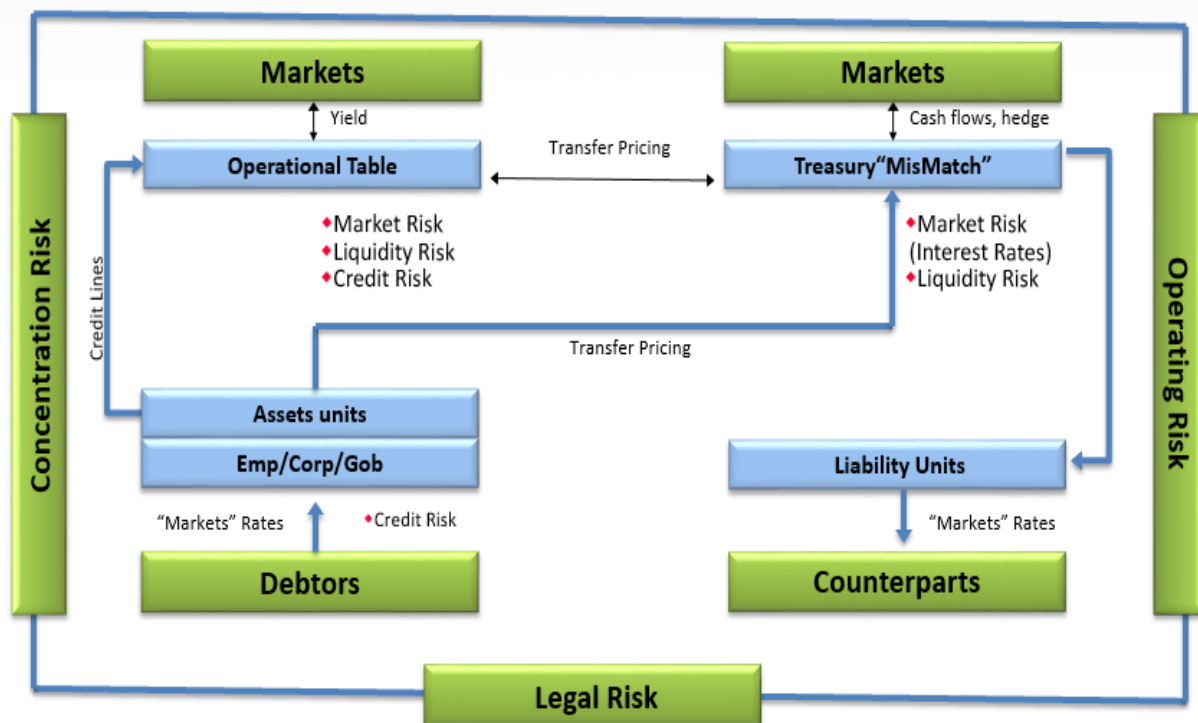


The methodological framework for risk management must facilitate and support measurement and monitoring of quantifiable risks, by assuring solid risk measurements to establish the Institution's risk appetite and generate value.

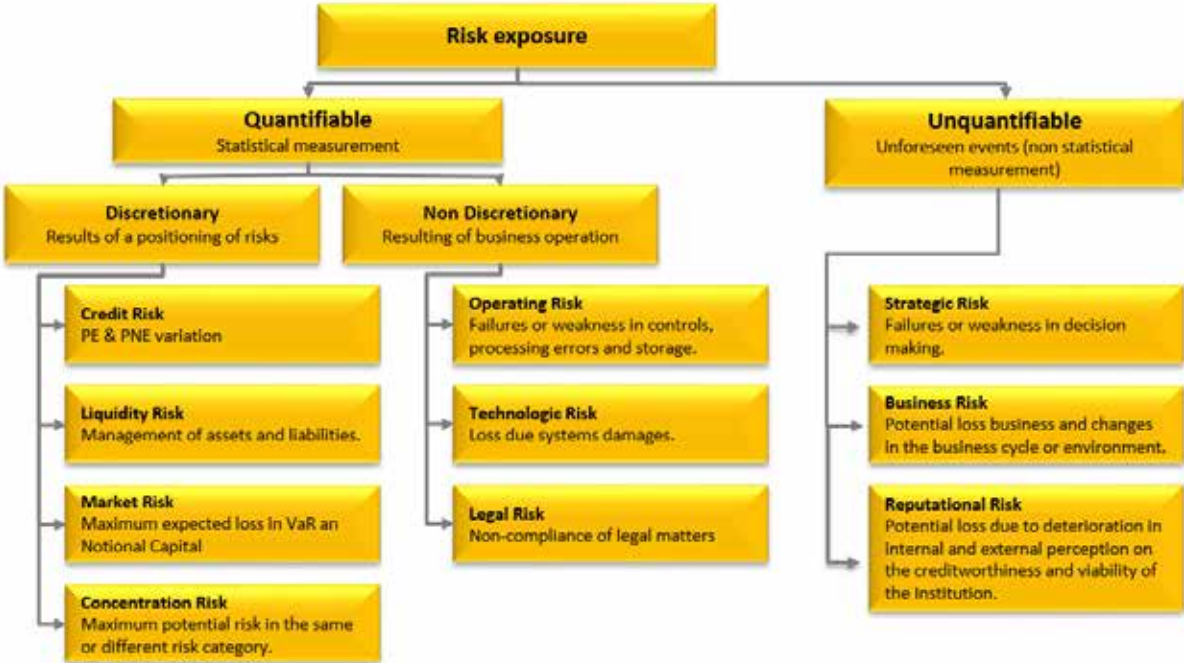
To assure that risk management is a support tool in decision-making, models and methodologies are established that allow for measuring, monitoring, and controlling the distinct types of risk to which the Institution is exposed. These risk measures must also contribute to the definition of business strategies and support the decision-making of the operation at the Institution.

A fundamental point of departure for establishing limits is the definition of a business model that describes exposure to the different types of risk that are generated by the different units that operate in the Institution.

- Treasury: It operates as a central unit that manages the Institution's resources. It is in charge of establishing transfer pricing, controlling liquidity levels, and controlling balance sheet risks. This unit incurs market, credit, and liquidity risks. In the case of the Nacional Financiera, it is also in charge of the liability unit.
- Operating desks: their main role is to generate revenues by operating on the different financial markets (money, currency, capital, and foreign currency bonds).
- Asset units: They are those that encompass the Institution's development activities and are derived from credit activities. These activities are the main generators of credit risk.

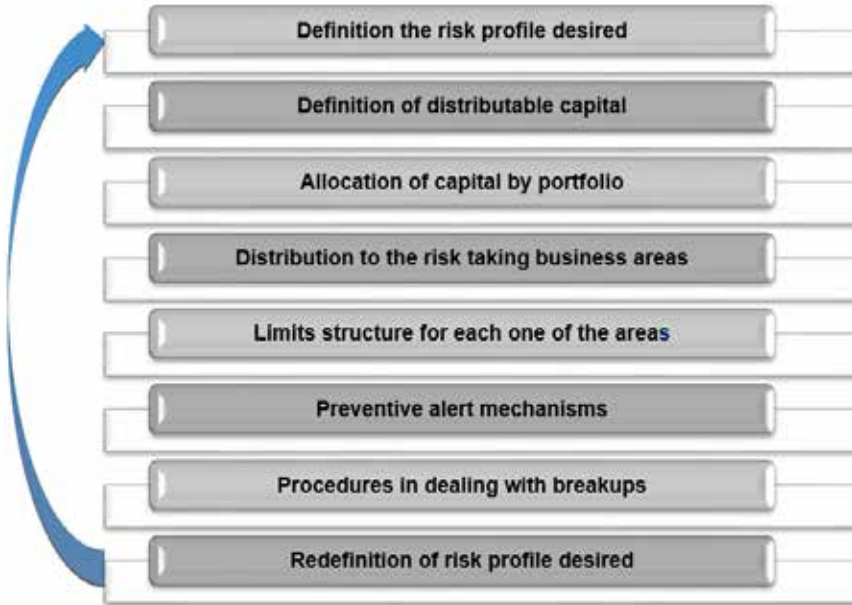


The types of risk to which the Institution is exposed are presented in the following diagram:



Pursuant to the foregoing, the Institution has a solid global and specific exposure limits on the distinct types of risk considering the consolidated risk, itemized by business unit, risk factor and cause.

Capital limits have a strong relevance. The following process is followed to determine limits:



The allocation process is derived from regulatory capital, based on what is set forth by capitalization rules. Starting with these concepts, distributable capital is determined, that is, the capital which the Institution has for dealing with the risk consumed in its operations.

Capital Limit Structure.

As part of the role of the DAR, Nacional Financiera, S.N.C., I.B.D. has a report structure that has mechanisms implemented in order for the results of the models (risk positions, VaR, Sensitivity analysis, and limit control, among other things) to be considered in the decision-making process, at both a tactical and strategic level.

Considering the foregoing, the capitalization level was placed at 13.20% at December 2016 year-end.



The Institution has a Contingency Financing Plan, which regulates the actions and coordination mechanisms required to deal with adverse liquidity events. That plan contemplates indicators defined for the purpose of following up and trying to foresee situations in which liquidity risk increases and comply with subsection VII of Article 81 of the Sole Bank Circular issued by the Commission.

NOTE 32. COMPREHENSIVE RISK MANAGEMENT

Risk management and follow-up.

National and international risk management regulations have observed an unprecedented evolution in these last years, by incorporating a preventive approach in the financial processes carried out by lending institutions, as well as the obligation of issuing internal guidelines that allow for establishing controls to prevent any economic loss due to the materialization of risks, either discretionary, non-discretionary or even those that are unquantifiable.

The Institution has implemented, as part of its controls and processes, the prudential provisions relating to risk management, credit management, and internal control management applicable to lending institutions, as well as the provisions issued by regulatory agencies in México in money

Discretionary quantifiable risks.

1. Market risk.

The Institution uses the Value at Risk (VaR) methodology to calculate the market risk of its trading and available-for-sale portfolios. The methodology that is being applied generally is historical simulation.

The most significant general principles are presented below:

- The confidence interval that is being applied to the calculation of VaR is 97.5% (considering the extreme left of the distributions of losses and gains).
- The base temporary horizon considered is 1 day.

A year of historical information of the risk factors is included for generating scenarios.

The following risk factors are considered: domestic and foreign interest rates, surcharges (spreads), exchange rates, indexes and prices of shares.

In addition to VaR information, sensitivity measures are calculated and stress tests are performed.

Effective July 2005, Back Testing is performed monthly to statistically validate that the market risk measurement model provides reliable results within the parameters selected by the Institution.

The limits on the values followed up on to date on a daily basis are:

- Value at risk: determined based on capital assigned to market risks.
- Nominative capital: based on the rules for capitalization requirements of Full-Service Banking Institutions and domestic lending companies, and Development Banking Institutions.
- Notional: these refer to maximum nominal values that can be held in position.
- Measure of maximum loss: this establishes a maximum loss limit against unfavorable trends on markets.

The average VaR of the year amounts to \$67.29, which represents 0.30% of net capital at December 2016 year end.

Markets	
VaR Amount \$67.29	
Trading	Treasury
VaR \$37.43	VaR \$29.86

2. Management of asset and liability.

Management of asset and liability refers to managing risks that affect the Institution's balance sheet. This consists of management techniques and tools necessary to identify, measure, monitor, control, and manage financial risks (liquidity and interest rate) that the institution's balance sheet is exposed to. Moreover, it is intended to maximize its yield adjusted by market risks and, therefore, enhance the use of the Institution's capital.

3. Liquidity risk.

Liquidity risk that affects a banking institution is generally classified in three categories:

- **Market liquidity risk:** It is the possibility of economic loss due to the difficulty of selling or covering assets without a significant reduction in their price. This type of risk is incurred as a result of drastic changes in interest rates when large positions are adopted in some instrument(s) or investments are made in markets or instruments for which there is no broad supply and demand on the market.
- **Funding liquidity risk:** This represents the difficulty of an institution in obtaining the necessary funds to pay its obligations, through the income generated by its assets or by acquiring new liabilities (deposits). This type of crisis is generally caused by a drastic, sudden impairment in the quality of assets that result in extreme difficulty to convert them in to liquid assets.
- **Liquidity risk due to a mismatch in cash flows:** the inability to meet present and future cash flow needs that affect the Institution's daily operation or financial conditions, as well as the potential loss due to the change in the structure of the Institution's balance sheet, due to the difference of periods between assets and liabilities.

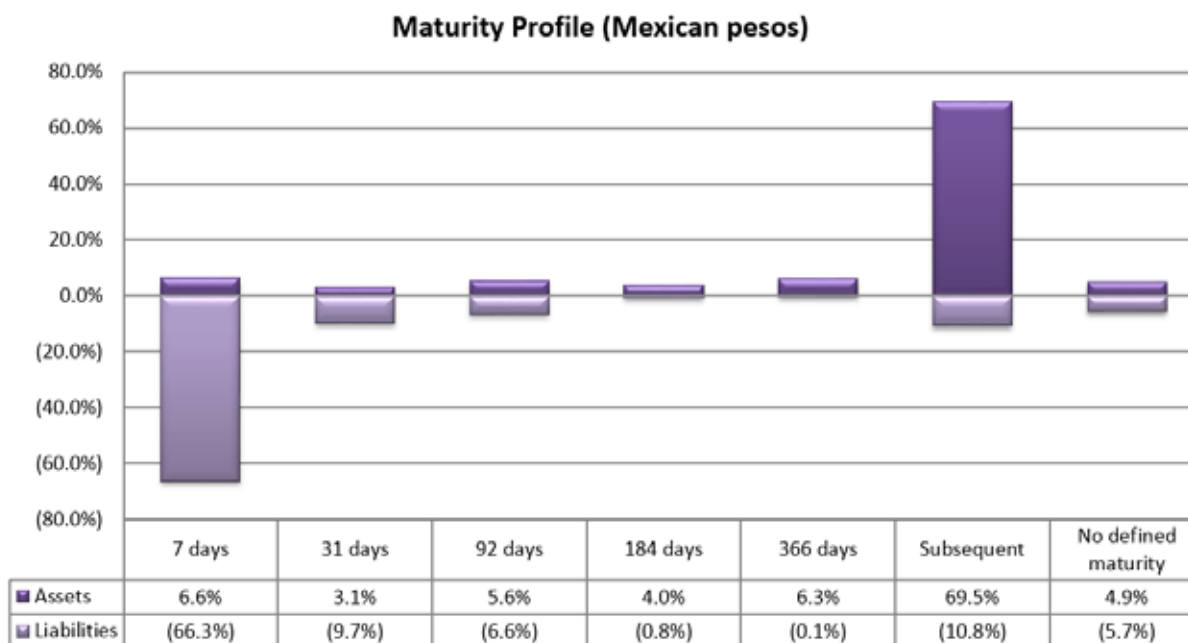
The Institution, in compliance with the Provisions of Comprehensive Risk Management, developed a Contingency Financing Plan, and liquidity stress scenarios, which set forth various measures to control, quantify, and follow up on the risks discussed above, as well as an action plan at an institutional level, in dealing with liquidity problems.

4. Local currency maturity profile.

Lending and borrowing transactions in local currency increased 13.0% during 2016, which is placed in for \$468,202 at December month end. Both balance sheet and memorandum account positions are considered, that is repurchase transactions (repos) and derivatives in the Maturity GAP, based on regulatory criteria. It is important to note that local currency deliverable on the trading of dollar forwards have been reclassified as liabilities, and the valuation of cross-currency swaps have been reclassified as assets.

Maturity ranges	2016			2015		
	Assets	Liabilities	Gap	Assets	Liabilities	Gap
Up to 7 days	\$ 31,084	\$ 310,287	(279,203)	\$ 57,889	\$ 259,909	(202,020)
Up to 31 days	14,357	45,647	(31,290)	11,908	65,713	(53,805)
Up to 92 days	26,096	31,106	(5,010)	30,481	11,253	19,228
Up to 184 days	18,714	3,630	15,084	21,746	551	21,195
Up to 366 days	29,647	403	29,244	30,818	3,755	27,063
Subsequent	325,430	50,420	275,010	230,253	44,601	185,652
With no defined maturity	22,874	26,709	(3,835)	31,394	28,707	2,687
Total	\$ 468,202	\$ 468,202		\$ 414,489	\$ 414,489	

The negative liquidity gap on the horizon of one month amounts to \$310,493, that is, \$54,668 more than the level recorded for \$255,825 the prior year.

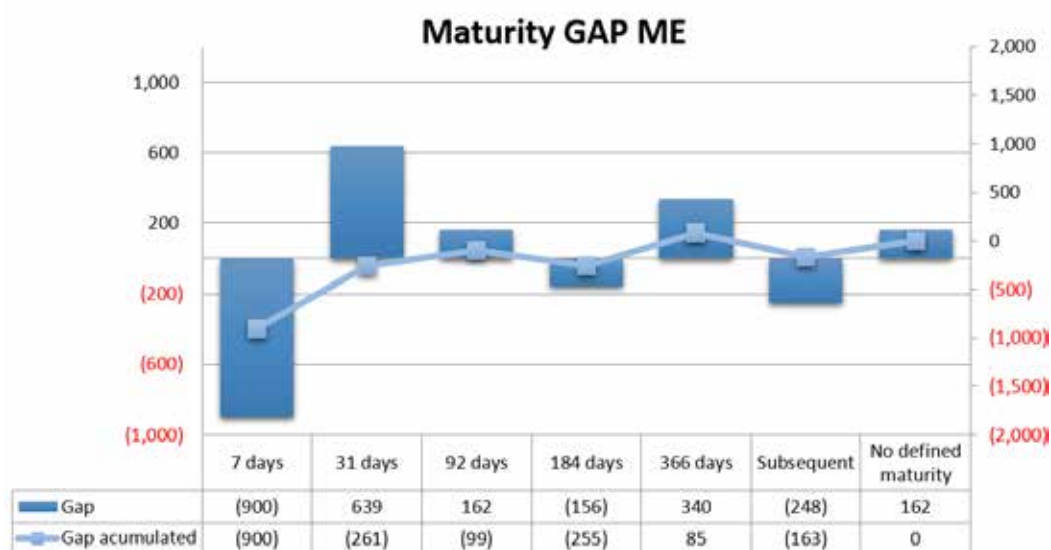


5. Foreign currency maturity profile.

Foreign currency lending and borrowing transactions at December 31, 2016 increased 37.3% in the course of the year, which resulted in a higher amount in assets and liabilities less than three months. Both balance sheet and memorandum account positions are considered, that is repurchase transactions (repos) and derivatives in the Maturity Gap, based on regulatory criteria.

Maturity ranges	2016			2015		
	Assets	Liabilities	Gap	Assets	Liabilities	Gap
Up to 7 days	\$ 1,690	\$ 2,590	(900)	\$ 2,237	\$ 1,612	625
Up to 31 days	1,213	574	639	351	407	(56)
Up to 92 days	1,193	1,031	162	69	624	(555)
Up to 184 days	79	235	(156)	193	226	(33)
Up to 366 days	471	131	340	47	37	10
Subsequent	2,009	2,256	(247)	1,932	2,060	(128)
With no defined maturity	162	-	162	137	-	137
Total	\$ <u>6,817</u>	\$ <u>6,817</u>		\$ <u>4,966</u>	\$ <u>4,966</u>	

In accordance with the contractual maturity of foreign currency assets and liabilities, and based on the amounts of the balance sheet at December 2016 closing, it is observed that there was liquidity for \$900 in the first 7 days of January 2016.



6. Estimate of gain or loss on advance sale.

In order to comply with the provisions of Article 81 of Section I, paragraph b), of the Provisions, the estimate on the gain or loss on the advance sale of assets in normal conditions and in extreme scenarios is presented below.

At December 2016 month end, upon considering crisis scenarios in corporate and investment trading portfolios a maturity, a loss would have been generated amounting to 156.85 million MXP equivalent to 0.9% of the value of the position, if there had been a situation similar to that at October 16, 2008.

Portfolio MXP	Position	Advance sale	Crisis scenarios					
			12/21/94	08/25/98	09/11/01	09/19/02	04/28/04	10/16/08
Corporate Trading	5,263.47	(0.12)	(0.12)	(0.69)	0.23	0.05	0.02	(0.00)
Investment to maturity	11,366.31	(131.27)	(90.25)	(117.75)	(0.65)	(20.46)	(131.27)	(156.85)

Upon considering crisis scenarios on the Cayman Island's available-for sale portfolios and the held-to-maturity bonds of London and Cayman Island, a loss could have been caused amounting to 71.53, equivalent to 0.9% of the value of the position, if there had been a situation similar to the crisis of 2008.

Portfolio MXP	Position	Early sale	Crisis scenarios					
			12/21/94	10/12/98	09/12/01	09/19/02	05/10/04	10/16/08
Available-for-sale	6,590.47	(199.50)	(18.62)	(199.50)	(230.21)	(92.45)	(77.10)	(55.70)
Investment to maturity	1,327.80	(23.10)	(6.38)	(56.25)	(4.80)	(23.10)	(20.71)	(15.83)

7. Credit risk.

Credit risk is defined as the likelihood that a counterparty or borrower fails to perform its credit obligations in due time and proper form. It further refers to the loss of value of an investment determined by the change in creditworthiness of any counterparty or borrower, without necessarily resulting in an omitted payment.

8. Expected Loss.

The expected loss on the loan portfolio is obtained by using the portfolio rating methodology set forth in Chapter V of the Provisions, in connection with the Loan Portfolio.

Pursuant to the reserve obtained under this methodology, the following assumptions are also established:

- The former employee portfolio is excluded to directly measure the effect of expected losses of the portfolio with private sector risk.
- The credit to the Trust is not considered as a contingent (nonperforming) portfolio for Risk Equity, since this Trust is responsible for managing its credit risk.
- No additional reserves are included.
- The portfolio of the financial agent is not considered since it is a portfolio without risk.
- It is considered a nonperforming portfolio. Moreover, in accordance with the portfolio rating methodology based on the expected loss, should an event of nonperformance materialize, it does not imply that the expected loss should be provided for at 100%

Under these assumptions, at December 2016 closing, the total portfolio is placed for \$214,062.9, whereas the expected loan portfolio loss amounts to \$2,720.3, equivalent to 1.27% of the rated portfolio and an equal percentage of the total portfolio.

Estimate of expected losses

Portfolio	Portfolio balance	Expected loss	% Expected loss
Unrated	\$ 157.7	\$ -	0.00%
Risk A	181,972.4	1,390.4	0.76%
Risk B	29,649.7	628.7	2.12%
Risk C	231.4	14.0	6.05%
Risk D	46.8	21.1	45.09%
Risk E	2,162.6	666.1	30.80%
Rated	214,062.9	2,720.3	1.27%
Total	\$ 214,220.6	\$ 2,720.3	1.27%

9. Unexpected losses.

The unexpected loss represents the impact that could be suffered by the Institution's capital derived from unusual loan portfolio losses, the level of coverage of this loss on capital, and reserves of an Institution is a solvency indicator adjusted by the risk thereof.

Effective December 2005, the estimate of unexpected loan portfolio loss operations is realized at the Institution, by using analytical and Monte Carlo simulation methodologies. As of that date, the stability of these measures and their behavior in the face of various changes in the environment has been observed to determine which of them should be used as the risk measure of Institution's loan portfolio.

In November 2007, the CAIR concluded that of the methodologies proposed for the estimate of the unexpected loan portfolio loss, the methodology with an economic approach is the best methodology that best conforms to the basic internal method of Basel II, based on:

- The similarity of concepts existing between the proposed economic methodology and capital requirement for the loan risk estimated starting with the basic approach of Basel II. This approach enables institutions to estimate the capital requirement with internal methods that is necessary to support their risk.
- The high correlation and similarity of the average capital requirement observed of internally applied methodologies of proposed unexpected loan portfolio loss during a year.

Moreover, the Institution considered that the unexpected loan portfolio loss should continue to be estimated monthly using the valuation and Monte Carlo methodologies, to have information in view of future changes of banking regulations in which portfolio market valuation is requested. These methodologies are applied over a one-year period with a 95% reliability level.

At December 2016 year-end, the estimate of the unexpected loss under the economic approach amounts to \$16,445. By the same token, the VaR of the credit amounts to \$19,424 million Mexican pesos and represents 9.07% of the exposed portfolio.

10. Counterparty risk and diversification.

Comprehensive control of counterparty risk is exercised at the Institution, by applying credit exposure limits established. These limits consider operations throughout all the balance sheet, that is, both on financial markets and in the loan portfolio. The methodology used is consistent with the General Rules for the Diversification of Risks in the Realization of Lending and Borrowing Operations, applicable to Lending Institutions.

At December 2016 closing, no loan risk is concentrated in any economic group above maximum financing limits.

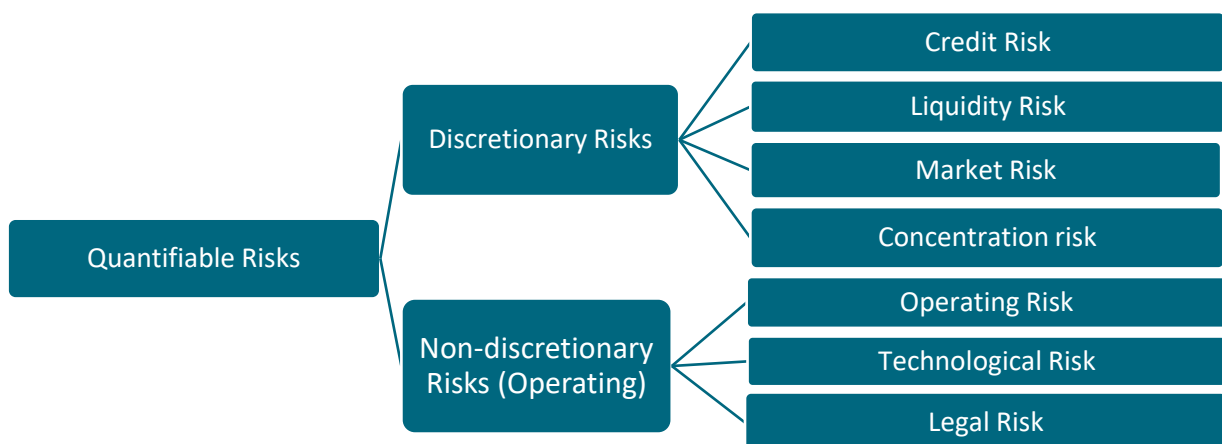
The following number of loans exceeds 10% of the basic capital individually:

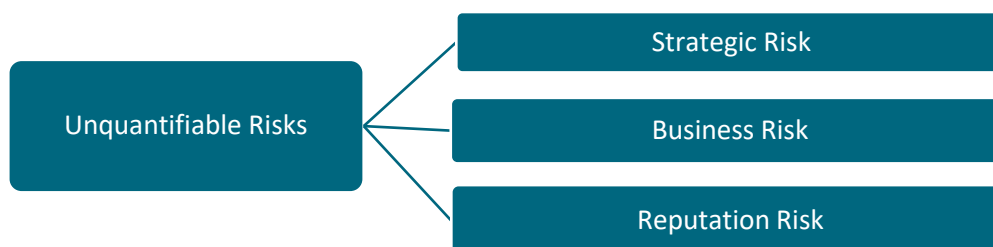
Number of loans	Total amount	Percentage of capital
34	\$ 210,035	957.84%

Financing with the three highest debtors or, if applicable, groups of persons that represent common risk amounts to \$56,410.

11. Operating and Non-quantifiable Risk.

The risks to which a financial institution are exposed to are classified in two large categories, quantifiable and unquantifiable. The unquantifiable risks, in turn, are divided into three types. This classification is shown below:





Non-discretionary risks, that is, the operating risk, are those derived from the business operation, but they are not a result of taking a risk position. These risks are defined below:

- Operating Risk: potential losses derived from internal control failures or deficiencies, errors in processing and storage transactions:
- Technological risk: potential losses on damages, interruption, alteration or failures derived from the use or dependence on hardware, software, systems, applications, networks, and any other information distribution channel in rendering services to the Institution's clients that result in processing and storage errors of transactions or in the information transmitted.
- Legal Risk: potential losses derived from the applicable legal and administrative provisions, unfavorable administrative and judicial resolutions handed down, as well as the application of sanctions in connection with the operations carried out by Institutions.

Unquantifiable risks are unforeseen events that cannot conform to a statistical base that allows for measuring potential losses which, among other things, are as follows:

- Strategic Risk: potential losses due to failures or deficiencies in decision-making, implementation of procedures and actions for the business model and the Institution's strategies to be carried out, as well as the unknown risks to which the Institution is exposed for undertaking its business activity, and affect the results expected for reaching the targets agreed upon by the Institution in its strategic plan.
- Business Risk: potential losses attributable to the risks inherent to the business and changes in the economic cycle or environment in which the Institution operates.
- Reputation Risk: potential losses in the development of the Institution's activity caused by the impairment in the perception that the distinct interested parties have, both internal and external, about its creditworthiness and viability.

The operating risk management and unquantifiable risks is to formally establish the standards and policies necessary to identify, measure, monitor, limit, control, inform, and disclose non-discretionary and unquantifiable risks systematically and efficiently, which must be adhered to by all areas of the Institution that are involved in activities that imply a non-discretionary or unquantifiable risk, as well as the purpose of assuring timely identification of capital requirements and resources derived from these risks.

The Institution has the following operating risk management and unquantifiable risk policies:

- The Risk Management information Sub-Department is responsible for defining the procedures for managing inherent operating and residual risks, events of economic losses, tolerance levels, risk limits, amounts of probable potential losses due to unfavorable judicial or administrative decisions of litigations in which the Institution is a plaintiff.
- None of the procedures defined for these risks may be modified or altered, only with the authorization of the Comprehensive Risk Management Committee and annually by the Board of Directors.
- The institution will have the necessary proof to manage non-discretionary and unquantifiable risks.
- Tools will be used that have been developed or acquired, if applicable, by the Institution to manage operating risk and unquantifiable risks.

Operating risk and unquantifiable risk strategy is to identify them, manage them, quantify them (if applicable), document how to mitigate them through risk controls by processes, by considering institutional experience that might impact or impair the solvency of the Institutional above minimum requirements, thereby helping to reach institutional goals and objectives. The information of these risks should also be disclosed to the Governing Bodies for timely decision-making. Moreover, foster a culture of managing these types of risks at the Institution.

The operating risk process is fundamental, and it is documented and certified in accordance with the quality management system under ISO 9001-2008 Standard, which assists in reaching the objective of managing operating risk to which the Institution is exposed.

The structure of the personnel who manage non-discretionary and unquantifiable risks have four elements, including the Information Risk Management Assistant Director.

In connection with the scope and nature of information and operating risk measurement systems and their reports, the Institution uses the institutional System named Operating Risk Tool, which incorporates information from the results obtained from operating risk monitoring. Moreover, everything is managed related to internal reports and regulatory reports (classifications and quantification).

Operating risk related reports (including technological and legal) are drawn up in the CAIR, through the "Risk Management and Follow-up Report" at least every quarter.

Methodologies, Limits, and Tolerance Levels.

Method for determining the Operating Risk Capital Requirement.

The Institution uses the Basic Indicator Method to calculate the capital requirement on its exposure to operating risk, by following the methodology described in the Provisions.

Non-Discretionary Risks: Operating Risk.

The methodology used for operating risk management (quantitative and qualitative analysis) is through an operating risk internal institutional model, which is based on a scorecard that considers five risk factors. The methodology is applied to the results of self-evaluations of the processes that describe the duties of the Institution and it allows for comparing the processes analyzed with two indicators, nature and efficiency, which have defined tolerance levels by risk factor and by indicator.

In addition, potential inherent risks of each process are identified, classified, and graded, based on the methodology defined by the Commission. The result is sent in an annual report named "Estimate of operating risk levels". The Commission's methodology provides product catalogues, process, line of business, type of risk, and a guide for calculating the frequency and impact of the inherent risk (without applying controls).

Considering the results obtained, potential risks inherent in the nine red area quadrant will be defined together with those responsible for the process to which it belongs, actions or additional controls to manage them.

The quantitative analysis is performed through operating risk loss events that occur at the Institution, whose information is furnished by the owners of the processes involved. These events are classified in accordance with the methodology defined by the Commission to draw up the Loss events due to operating risk" and "Update of loss events due to operating risk" regulatory reports. The Commission's methodology provides product catalogues, process, line of business, and type of risk.

An operating risk limit was defined for monitoring loss events, considering the positive net income of three years, considering methodologies and the Commission's comments.

Non-Discretionary Risks: Technological Risk.

The technological risk methodology for identifying, quantifying, and managing this risk is carried out by informatics, and it is based on five indicators, which are network security, detection and blocking of viruses, availability of critical and non-critical services. Reports are submitted with the CAIR as a risk monitoring control on at least a quarterly basis.

Its monitoring is monthly and it is carried out by comparing the levels obtained in each indicator that considers the events reported by user areas vs. tolerance levels agreed upon between informatics and those areas (Meta).

The information of this risk is inputted by informatics directly in the operating risk tool.

Legal risk.

There is an internal methodology for estimating the record of potential legal risk losses, based on the expectations of specialists of having a favorable ruling handed down and classifying them into five ranges.

- without sufficient elements
- high
- moderate
- considerable
- low

The methodology is applied by the Adversarial Juridical and Credit Department, whose personnel identify, quantify, and manage the legal risk. Reports are submitted with the CAIR as a risk monitoring control on at least a quarterly basis.

The results of potential legal risk losses are grouped and reported to the CAIR at least quarterly, by type of litigation which are as follows:

- Labor Nature
- Litigation Portfolio
- Trust
- Mercantile
- Treasury and securities trading

Risks in the Institution's capital assets

Unquantifiable risks are those derived from losses or unforeseen external events that cannot be associated with a likelihood of occurrence and the economic losses caused can be transferred to external risk taking entities.

Type of risk	Definition	Example
Loss	Loss risk due to catastrophic events of the nature that they can interrupt the operation or affect the capital assets of the Institution.	Fire, earthquake, volcanic eruption, hurricane, among other things.
External	Risk of loss caused entities not related to the Institution.	Vandalism, sit-ins, etc.

This type of risk is followed up on by considering the following criteria:

Inventory	Control measures	Economic impact
Capital Assets	Institutional Capital Asset Insurance Program	Premium payment
Repossessed Assets	Institutional Capital Asset Insurance Program	Deductibles in the event that they should materialize.

During 2016, policies covered the damages that eventually occur in national territory and abroad of the tangible and intangible assets (all types of software or packages of programs, licenses, permits, information technology, and databases), which generally include material damages, civil liability, Accidental breakage of glass including lighted ads, robbery and/or violent or non-violent assault, robbery of money and bank securities, electric, electromechanical, electronic, electromagnetic, and fixed or mobile telephony equipment, boilers and equipment subject to pressure, breakage of machinery, contractor equipment, goods in transit (transportation), works of art and difficult or impossible to replace objects, money and securities, weapons and security equipment, personal accidents, employee disloyalty and terrorism. Moreover, there is a policy that covers the vehicle fleet.

Unquantifiable risks.

The methodologies implemented concur with the stipulations of the Provisions. A brief description of them is provided below:

- Strategic risk.- The institution has a methodology based on defining documenting, and following up on executive management strategies, which are defined and approved every year, as well as presented to the Board of Directors at least every quarter, for decision-making and mitigation of the risks detected.
- Business risk.- Four indicators were defined as a methodology for managing this risk, which helps to identify the possible materialization of the risks that might affect the Institution, due to the movements in the financial environment and the economic cycle. These indicators are monitored through risk reports every month.

- Reputation risk.- A Communication Plan was defined for managing this risk of the Social Communication Department (plan, which applies and monitors the Social Communication Department. That plan considers the attention of the minimum requirements issued by the Commission in the reputation risk Provisions. The Social Communication Department follows up on the events that affect the negative perception that exists inside or outside of the Institution. This risk is reported to the CAIR as a control of this risk monitoring on at least a quarterly basis.

Operating risk results.

Results of self-evaluations.

The result obtained from the Institution's most relevant processes in terms of their nature at December 2016 month-end is as follows:

Name of the process	Nature Indicator */	Tolerance level
Treasury management	111.50	High Risk
Securities and cash custody and management	98.84	High Risk
Cash flow management and control	92.57	High Risk
General cashier's office	90.50	High Risk
Foreign exchange market	89.29	High Risk
Money market	88.29	High Risk
Capitals market	85.31	High Risk
Recovery of second tier portfolio	84.01	High Risk
Recovery of first tier portfolios, emerging programs, and former employees	79.32	Medium High Risk
Front office financial agent	78.50	Medium High Risk
Derivatives market	75.95	Medium High Risk
Credit control desk operation	70.00	Medium High Risk
Back office financial agent	69.61	Medium High Risk
It keeps securities and central file	65.99	Medium High Risk
Automatic guarantee management	65.04	Medium High Risk
Trustee	63.24	Medium High Risk
Financial and accounting information and preparation of financial statements	62.00	Medium High Risk
Electronic product management	61.61	Medium High Risk
Expense operation	57.30	Medium High Risk

*/ The higher the score, the more critical in terms of the nature of the process.

The result obtained at December 2016 closing of the most relevant processes that describe the duties of the Institution, in terms of efficiency, is as follows:

Name of the process	Efficiency indicator */	Tolerance level
Financial and accounting information and preparation of financial statements	44.75	Medium Risk
Foreign exchange market	39.29	Medium Risk
Derivatives market	37.04	Medium Risk
Treasury management	36.63	Medium Risk
Securities and cash custody and management	36.50	Medium Risk
Trustee	35.33	Medium Risk
Front office financial agent	35.00	Medium Risk
Recovery of second tier portfolio	34.76	Medium Risk
Expense operation	34.25	Medium Risk
Electronic product management	33.23	Medium Risk
Recovery of first tier portfolios, emerging programs, and former employees	32.95	Medium Risk
Capitals market	32.39	Medium Risk
Back office financial agent	32.14	Medium Risk
Money market	31.87	Medium Risk
Cash flow management and control	31.00	Medium Risk
General cashier's office	30.85	Medium Risk
Credit control desk operation	28.70	Medium Risk
Automatic guarantee management	27.00	Medium Risk
It keeps securities and central file	26.67	Medium Risk

Note.- The higher the score, the more critical in terms of the efficiency of the process.

No inherent potential operating risk was defined nor recorded in a red area in 2016, that is, area nine (high frequency and high impact); therefore, the institution complied with the established risk limit.

Results of Economic Loss Events.

Forty-seven operating loss events were recorded in 2016, with a probable impact of 10.08 million mexican pesos. The monthly average was four events with an amount of 0.84 million mexican pesos.

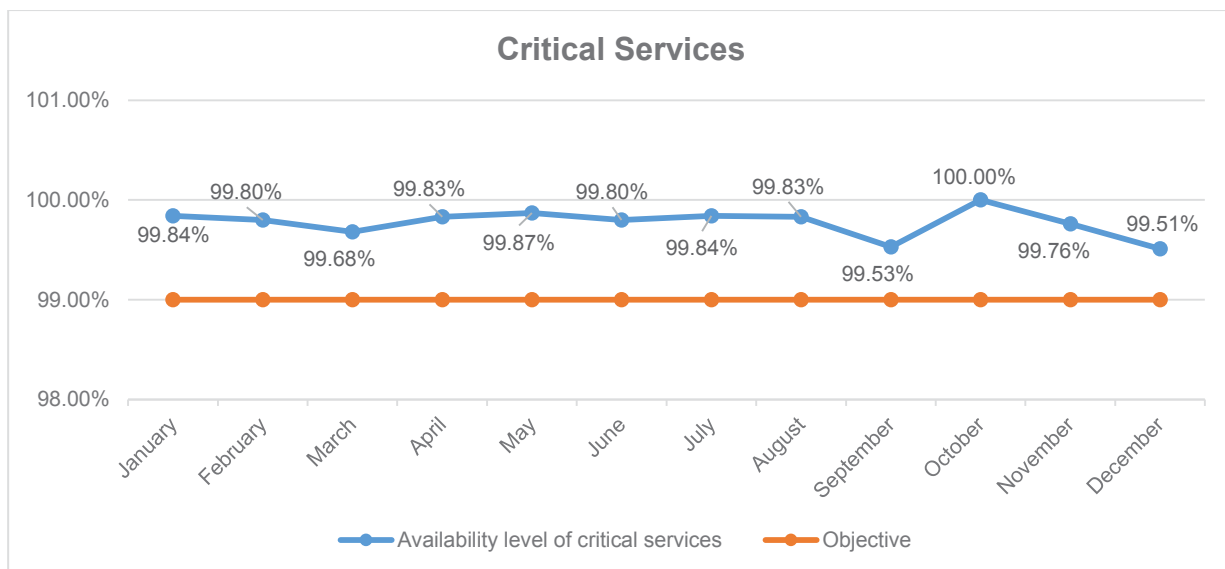
Quarter	Number of events	Likely economic impact	% of the LEI in each quarter	Average amount per month event
First	8	0.41	4.04%	0.05
Second	12	0.12	1.17%	0.01
Third	17	8.42	83.53%	0.50
Fourth	10	1.13	11.26%	0.11
Total	47	10.08	100.00%	

The consumption of the limit of economic loss events at every month end of 2016 was within the established parameters, except for July in which there was an exposure amounting to \$6.5.

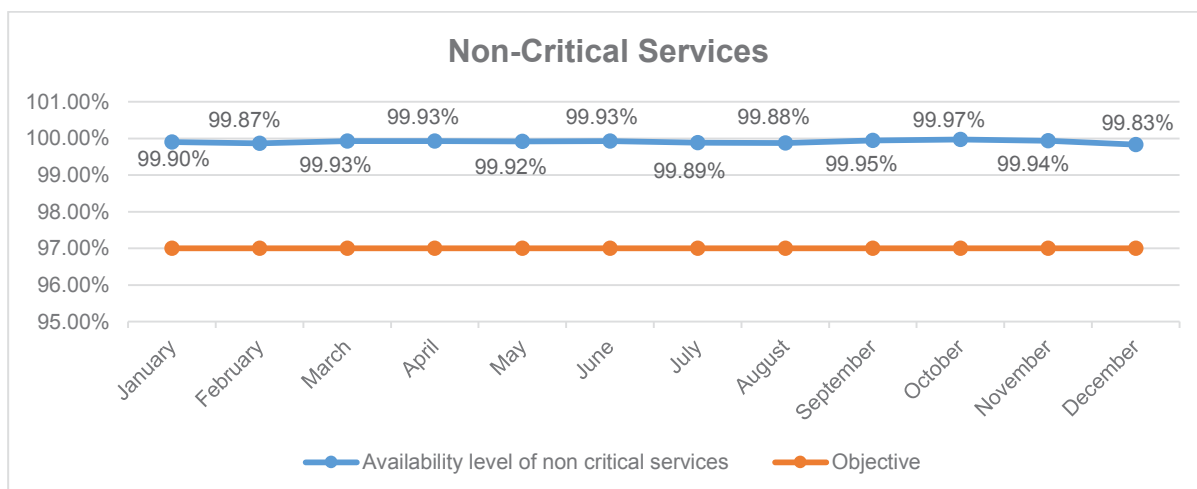
Result of Technological Risk Indicators.

During the twelve months of 2016, the network level indicator had zero intrusions. The recovery of critical services indicator under disaster drill had 100% behavior. Moreover, the detection and blocking of viruses from the network had zero impacts. The quarterly and monthly average of these three risk indicators placed in the defined goal.

The behavior obtained of the availability of critical services indicator in the twelve months of 2016 is as follows:



The behavior obtained of the availability of non-critical services indicator in the twelve months of 2016 is as follows:



The five technological risk indicators were found within the goals established for management of this Risk.

The quarterly average and monthly average behavior of the Availability of critical services and non-critical services Availability indicators in 2016 were as follows:

T. R. Indicator Description	1st Quarter 2016	2nd Quarter 2016	3rd Quarter 2016	4th Quarter 2016	2016 annual average
Availability level of critical services	99.77%	99.86%	99.73%	99.76%	99.78%
Availability level of non-critical services	99.90%	99.93%	99.91%	99.91%	99.91%

The quarterly and monthly average of the availability level of critical and non-critical services were within the established goals.

Result of Legal Risk.

At December 2016 year end, the status of recording potential legal risk losses is as follows:

Type of lawsuit	Contingency	Provision	Provision / Contingency	Income (loss)	Income or loss / Provision
Total (1+2+3+4)	134.47	50.14	37.29%	15.96	31.83%
1) Labor Nature	36.41	22.40	61.52%	15.63	69.78%
2) Litigation Portfolio	10.68	9.44	88.39%	0.33	3.50%
3) Trusts	87.38	18.30	20.94%	0.00	0.00%
4) Treasury and securities trading	0.00	0.00	0.00%	0.00	0.00%

Comparative results with the prior year:

1. The labor portfolio contingency reports an amount of \$36.41 million Mexican pesos, which had a 50.45% variation with respect to the prior year, which is equivalent to an amount of \$12.21. The provision reports an amount of \$22.40 million Mexican pesos, which had a 88.39% variation with respect to the prior year, which is equivalent to an amount of \$10.51. The movement in Contingency is derived mainly from the beginning of three labor lawsuits, the update of five cases in the expectations of having a favorable ruling handed down for the institution and the corresponding restatement in the amount of the suit by operation of law. The movement in Provision is due mainly to the beginning of two labor lawsuits expected to have a low favorable ruling handed down and the update of five cases expected to have a favorable ruling handed down for the Institution.

2. The litigation portfolio reports an amount of \$10.68, which had a 62.67% variation with respect to the prior year, which is equivalent to an amount of \$17.93. The litigation portfolio reports an amount of \$9.44, which had a 3.62% variation with respect to the prior year end, which is equivalent to an amount of \$0.33. The movement in Contingency and Provision is due mainly to the satisfactory conclusion of a legal proceeding and the restatement of the amount demanded in a case.
3. The trust contingency portfolio reports an amount of \$87.38, which had a 5.71% variation with respect to the prior year end, which is equivalent to an amount of \$4.72. The provision of Trusts reports an amount of 18.30 million mexican pesos, which had a 0.11% decrease, which is equivalent to an amount of \$0.02 million mexican pesos. The movement in Contingency and Provision is mainly due to the volatility of the MXP/USD exchange rate, a legal proceeding concluded satisfactorily, and the incorporation of two new cases with a high perspective of success.

Unquantifiable risks.**Risks in the applications to the Institution's capital assets.**

Three claims were reported in 2016 that affected the institution's capital assets in the field of electronic and miscellaneous equipment, with an estimated amount of \$0.01.

Strategic Risk.

The behavior of meeting the goals of executive management has been followed up on at least quarterly in 2016, to identify the main risks expertly, in order to mitigate them and eventually make decisions that do not lead to noncompliance with the goals of the Institution.

Business Risk.

Defined indicators for managing this risk were monitored in 2016, through risk reports on market, concentration, liquidity, guarantees, and credit.

Reputation risk.

The Social Communication Department met the minimum reputation risk requirements issued by the Commission in the Provisions in 2016. Events that affect the negative perception existing both internally and externally were monitored monthly. The positive and negative notes are analyzed through printed, electronic communication channels, as well as internet portals and state information.

General Internal Control Rules in a Federal Public Administration environment.

The agreement on which the Internal Control Provisions are issued and the General Internal Control Administrative Application Manual (The Agreement) issued by the Ministry of Public Office, announced in the Official Daily Gazette on July 12, 2010, whose most recent update was on May 2, 2014, presents the requirements that agencies and government entities of the Federal Public Administration and the Office of the Attorney General should observe for the reduction and simplification of administrative regulation of Internal Control issues.

The documents of "2015 fourth quarter Risk Management Work Plan Progress Report" and "Annual Report of Institutional Risk behavior at a Strategic level at 2015 year end, contained in the regulation of Internal control matters issued by the Ministry of Public Office (SFP)" were drawn up and formalized in the first quarter of 2016. Moreover, they were submitted to the Audit Committee at its meetings of February and March 2016, respectively.

In addition, the General Director of the Institution Informed the Head of the Internal Control Organ of the Institution on April 20, 2016 that due to the modifications of the standards that govern development banks issued by the Commission, beginning this year, the policies, guidelines, and procedures will be applied for Comprehensive Risk Management and for the Internal Control System, pursuant to the particularities that the Institution has as a development bank and the standards that govern it, without contravening the Provisions contained in the agreement.

The information concerning the leveraging ratio is disclosed with amounts at December 2016, in compliance with the Resolution that modifies the general provisions applicable to lending institutions, namely, Article 2 Bis, 120, Articles 180, 181, and exhibit 1-O Bis, published in the Official Daily Gazette on June 22, 2016.

TABLE I.1
STANDARD FORM FOR LEVERAGE RATIO DISCLOSURE

REFERENCE	CAPTION	AMOUNT
On-Balance Sheet Exposure		
1	On-balance sheet items (excluding derivative financial instruments and repurchase operations and securities lending, but including collaterals received and recorded on the balance sheet).	492,525
2	(Amounts of assets deducted to determine capital Tier 1 of Basilea III)	- 3,413
3	Exposure on balance sheet (net) (excluding derivative financial instruments and SFT, sum of lines 1 and 2)	489,112
Exposure to derivative financial instruments		
4	Current replacement cost associated with all transactions with derivative financial instruments (net of the allowable cash variation margin)	3,205
5	Amount of the additional factors by future potential exposure, associated to all transactions with derivative financial instruments.	2,490
6	Increase by collateral contributed in transactions with derivative financial instruments when such collateral is written-off from the balance sheet according to the operating accounting framework.	N.A.

TABLE I.1
STANDARD FORM FOR LEVERAGE RATIO DISCLOSURE

REFERENCE	CAPTION	AMOUNT
On-Balance Sheet Exposure		
7	(Deductions to accounts receivable by margin of variation in cash contributed in transactions with derivative financial instruments)	-
8	(Exposure to derivative financial instruments on behalf of clients, in which the liquidating partner does not grant its guarantee in case of non-compliance with the obligations of the Central Counterparty)	N.A.
9	Effective adjusted notional amount of the underwriting credit derivatives.	N.A.
10	(Compensations made to the adjusted effective notional of the credit derivative financial instruments underwritten and deductions of the additional factors by the credit derivative financial instruments underwritten)	N.A.
11	Total exposure to derivative financial instruments (sum of lines 4 to 10)	5,695
Exposure to securities financing operations		
12	Gross SFT assets (without compensation recognition), after adjustments for sales transactions.	22,297
13	(Accounts Payable and Receivable for offset SFTs)	- 22,277
14	Exposure Risk of Counterparty by SFT	161
15	Exposure by SFT on behalf of third parties	-
16	Total exposure for securities financing operations (sum of lines 12 to 15)	181
Other exposures off-balance sheet		
17	Off-balance exposure (gross notional amount)	112,816
18	(Translation adjustments to credit equivalents)	- 101,534
19	Off-balance items (sum of lines 17 and 18)	11,282
Capital and total exposures		
20	Capital Tier 1	22,657
21	Total exposures (sum of lines 3, 11, 16 and 19)	506,270
Leverage ratio		
22	Leverage ratio of Basilea III	4.5%

TABLE II.1
COMPARATIVE OF TOTAL ASSETS AND AJUSTED ASSETS

REFERENCE	DESCRIPTION	AMOUNT
1	Total assets	515,075
2	Adjustment for investments in the capital of banking, financial, insurance or commercial entities that are consolidated for accounting purposes, but are outside of the scope of regulatory consolidation.	- 3,413
3	Adjustment for trust assets recognized on-balance sheet under the accounting framework but excluded from the measurement of the exposure to the leverage ratio.	N.A.
4	Derivative financial instruments adjustment.	5,442
5	Repurchase and securities lending operations adjustment.	- 22,116
6	Adjustment for recognized items off-balance-sheet.	11,282
7	Other adjustments	-
8	Exposure of the leverage ratio	506,270

TABLE III.1
RECONCILIATION BETWEEN TOTAL ASSETS AND ON-BALANCE SHEET EXPOSURE

REFERENCE	DESCRIPTION	AMOUNT
1	Total assets	515,075
2	Derivative financial instruments transactions	- 253
3	Repurchase and securities lending transactions.	- 22,297
4	Trust assets recognized in the balance sheet under the accounting framework, but excluded from the measure of exposure to the leverage ratio.	N.A.
5	On-balance sheet exposure	492,525

TABLE IV.1
MAIN CAUSES OF THE MOST IMPORTANT VARIATIONS OF THE
ELEMENTS

(NUMERATOR AND DENOMINATOR) OF LEVERAGE RATIO

CONCEPT/QUARTER	Dec-16
Core capital	22,657
Adjusted assets	506,270
Leverage Ratio	4.5%

NOTE 33. RESTATEMENT OF 2015 FINANCIAL STATEMENTS

During November and December 2016, the Institution recognized certain accounting corrections retrospectively in the financial statements for the year ended December 31, 2015 with the following effects:

	Balances At December 31, 2015	Restatement effects	Restated balances at December 31, 2015
ASSETS			
Held-to-maturity securities	(a) \$ <u>12,894</u>	\$ <u>30</u>	\$ <u>12,924</u>
Other assets	(b) \$ <u>1,322</u>	\$ <u>(148)</u>	\$ <u>1,174</u>
LIABILITIES			
Negotiable instruments issued	(b) \$ <u>68,899</u>	\$ <u>(54)</u>	\$ <u>68,845</u>
Deferred credits and Advance payments from customers	(b) \$ <u>144</u>	\$ <u>(94)</u>	\$ <u>50</u>

	<u>Balances at December 31, 2015</u>	<u>Restatement effects</u>	<u>Restated balances at December 31, 2015</u>
STOCKHOLDERS' EQUITY			
Capital gains:			
Net income	(a) \$ 1,254	\$ 30	\$ 1,284

- (a) Recognition of interest derived from the gain on inflation of CBICS, which the system was undervaluing in 2015.
- (b) Presentation in conformity with the criterion “**A-2 Application of Particular Standards**” in paragraph 38 of Exhibit 33 of the Sole Circular of Banks.

NOTE 34. NEW ACCOUNTING PRONOUNCEMENTS

A series of Financial Reporting Standards (FRS) and Improvements to FRS issued by the CINIF in December 2015 and 2016 are described below, which will go into effect in the year indicated. These FRS and Improvements to FRS are considered not to have a significant application in the consolidated financial information presented by the Institution.

2017

Beginning January 1, 2017, the following improvements to FRS were issued:

FRS B-13 “Events subsequent to the date of the financial statements”, FRS B-6 “Statement of financial position”, FRS C-19 “Financial instruments payable”, and FRS C-20 “Financial instruments receivable” If an agreement is reached to maintain long-term payments of a liability contracted with those payment conditions and which have fallen into default at the date on which the financial statements are authorized to be issued, that liability is allowed to be classified as a long-term item at the date of the financial statements, and its early application is permitted for fiscal years beginning January 1, 2016.

FRS D-3 “Employee benefit” This standard is modified to establish that, as a basic principle, the discount rate to be used in the determination of the present value of long-term labor liabilities must be a free market rate, or a credit risk with a very low risk, which represents the value of money in time. Consequently, either the government bond market rate or high quality corporate bonds might be used indistinctly in absolute terms on a deep market, provided that high quality corporate bonds meet the requirements set forth in Appendix B “Application guides”, B1 “Guide for identifying issues of high quality corporate bonds in absolute terms on a deep market”. Its early application is permitted.

2018

Beginning January 1, 2018, the following FRS will go into effect:

FRS B-17 “Determination of fair value” This standard defines fair value as the starting price that would be received for selling an asset or paid for transferring a liability in an orderly transaction between market participants at the valuation date (that is, a current value based on the starting price). Determining fair value requires considering:

- The particular asset or liability that is being valued;
- The higher and best use of the asset for a nonmonetary asset, and if the asset is used in combination with other assets and on an independent base.
- The market on which an orderly transaction would take place for the asset or the liability.
- The appropriate valuation technique or techniques for determining fair value, which must maximize the use of relevant observable input data and minimize unobservable input data.

FRS C-2 “Investment in financial Instruments (FI)” The main change in this standard is the classification of FIs in which investments are made. The concept of intent of acquisition and use of an investment in an FI is ruled out to determine its classification. The business model concept is adopted in its place of management of investments in FIs in order to cash flows, which can be to obtain a contractual return of an FI on the collection of contractual yields and /or sale or obtaining gains on buying and selling them to classify the various FIs. A reclassification of investments in financial instruments is not permitted between their categories (receivable, debt at fair value, and marketable), unless the business model of the entity is changed, which seldom occurs.

FRS C-3 “Accounts receivable” The main changes consist of specifying that:

- Accounts receivable based on a contract represent a financial instrument.
- The allowance for doubtful commercial accounts is recognized from the time at which the revenue is accrued based on expected loan losses.
- It sets forth that the value of money in time should be considered from the initial recognition. Accordingly, if the effect of the present value of the receivable is significant, it should be adjusted based on present value; and
- Present an analysis of the change between the opening balance and the final balance of the allowance for doubtful accounts.

FRS C-9 “Provisions, contingencies and commitments” The term probable was adjusted in the definition of liability and the term of virtually unavoidable was eliminated. The first - time application of this FRS does not generate accounting changes in the financial statements of the entities.

NIF C-10, "Derivative financial instruments and hedge ratios"

- Hedge ratios are required to be aligned with the risk management strategy for which they qualify as hedge ratios. Otherwise, they would not qualify as such, and they might not be recognized as hedge ratios.
- The restriction was eliminated of being able to establish a hedge ratio of assets and liabilities valued at fair value.

- Specific measurements are eliminated (between 80% and 125% with respect to the variations of the hedged item) to determine if a hedge is effective, and any ineffectiveness is immediately recognized in income;
- The hedge ratio is only discontinued if the hedge instrument or hedged item no longer exist or if the risk management strategy changes, which is unusual and seldom;
- Hedge proportion is required to be rebalanced if there is ineffectiveness, either by increasing or decreasing the hedged item or the hedge instrument.
- Existing embedded derivative financial instruments are not permitted to be separated when the host instrument is a financial asset; and
- A net income and expense position is permitted to be designated as a hedged item, while that designation reflects the risk management strategy of the entity.

FRS C-16 “Impairment of financial instruments receivable” Determine when and how expected losses must be recognized for Impairment of Financial Instruments Receivable. Those losses must be recognized when credit risk increases and it is concluded that part of the future cash flows of the Financial Instruments Receivable will not be recovered. It further proposes that the expected loss be recognized based on historical experience of loan losses, current conditions, and reasonable and sustainable forecasts of the different quantifiable future events that might affect the amount of future cash flows recoverable from those Instruments. This implies that estimates should be made that must be adjusted periodically, based on the experience gained. Moreover, it has to be determined how much and when are expected to recover for Financial Instruments Receivable that accrue interest, since the recoverable amount must be at its fair value.

FRS C-19, "Financing instruments payable" This FRS sets forth:

- The possibility of subsequently valuing certain financial liabilities at their fair value subsequent to their initial recognition when certain exceptional conditions are met.
- Value long-term liabilities at their present value in their initial recognition, considering their value in time, when their term exceeds one year or outside of normal credit terms; and
- Restructuring a liability without substantially modifying future cash flows to pay it in full, the costs, and fees disbursed in this process will affect the amount of the liability and they will be amortized at a modified effective interest rate, instead of being allocated directly to net income or loss.

FRS C-20 “Financing instruments receivable” This standard specifies the classification of financial instruments in assets, based on the business model:

- If a gain is generated through a contractual return, predetermined in a contract, they are recognized at their amortized cost;
- In addition, if they are used to generate a gain based on their buying and selling, they are recognized based on their fair value. The embedded financial instrument, which modifies the flows of the principal and interest of the host instrument, will not be separated, but rather everything will be valued at their fair value, as if it were a marketable financial instrument.

NOTE 35. AUTHORIZATION TO ISSUE THE FINANCIAL STATEMENTS

The officers who subscribe the consolidated financial statements authorized those statements and their corresponding notes to be issued on February 15, 2017.

These notes are part of the consolidated financial statements at December 31, 2016 and 2015.



Dr. Jacques Rogozinski Schtulman
Chief Executive Officer



Dr. Federico Balli Gonzalez
Associate General Director of Administration and
Finance



C. P. Sergio Navarrete Reyes
Accounting and Budget Director



**NACIONAL FINANCIERA, S. N. C.,
Development Banking Institution and Subsidiaries**

**INDEPENDENT AUDITORS' REPORT
AND CONSOLIDATED FINANCIAL STATEMENTS
AT DECEMBER 31, 2016 AND 2015**

The background of the top half of the page is a complex digital graphic. It features a dark blue and purple color palette. Scattered throughout are various numbers (0-9) in different colors and sizes, some appearing to float or be part of a network. There are also 3D cubes and rectangular blocks in shades of purple and pink, some of which are semi-transparent. The overall effect is one of a dynamic, data-driven environment.

EXHIBIT

NACIONAL FINANCIERA
ANNUAL REPORT 2016

Directory of Regional
and Overseas Offices



Regional Offices:

NORTHWEST REGIONAL OFFICE

Said Saavedra Bracamonte
(Director)

Blvd. Eusebio Kino No. 309
Torre Hermosillo 5° piso
Col. Country Club
Hermosillo, Sonora.
C.P. 83010
Tel: 01-662-289-2301 a la 2303
E-mail: ssaavedra@nafin.gob.mx

SOUTHEAST REGIONAL OFFICE

María Teresa Cavazos Samia
(Director)

Calle 17 No. 135
Col. México
Mérida, Yucatán.
C.P. 97125
Tel: 01 999 948-4878, 4883 y 4884
E-mail: mcavazos@nafin.gob.mx

NORTHEAST REGIONAL OFFICE

Luis Roberto Reyna Ortiz
(Director)

Av. El Roble No. 300, Edificio Torre Alta, P.B. Esq. Gómez Morín
Col. Valle del Campestre
San Pedro Garza García, Nuevo León.
C.P. 66265
Tel: 01-81-8173-1200 y 1201
E-mail: lrreynao@nafin.gob.mx

LONDON BRANCH

Pedro Guerra Menéndez
(Commissioned in substitution for the absence of the owner)

28th Floor, 30 St. Mary Axe
London EC3A 8BF
Tel: 00 (44) 020-7469-4123
Fax: 00 (44) 020-7469-4122

WESTERN REGIONAL OFFICE

Jorge Alberto Guerra Márquez
(Director)

Rubén Darío No. 1109-5A,
Col. Providencia
Guadalajara, Jalisco.
C.P. 44620
Tel: 01-33-3648-5501 y 5502
E-mail: jaguerra@nafin.gob.mx

CENTRAL REGIONAL OFFICE

David Garibay Mendoza
(Director)

Insurgentes Sur 1971, torre 4, piso 11, Plaza Inn
Col. Guadalupe Inn, Delegación Álvaro Obregón
México, Ciudad de México
C.P. 01020
Tel: 01-55-5325-6132
E-mail: dgaribay@nafin.gob.mx

2016



nacional financiera
Banca de Desarrollo