

NACIONAL FINANCIERA, S.N.C.

ANNUAL REPORT 2017



nacional financiera
Banca de Desarrollo



BOARD OF DIRECTORS AND COMMISSIONERS AS OF DECEMBER 31, 2017

BOARD MEMBERS SERIES "A"	
HOLDERS	DEPUTIES
JOSÉ ANTONIO GONZÁLEZ ANAYA Minister of Finance and Public Credit and Chairman of the Board of Directors	MARIO GOVEA SORIA Head of Development Banking Unit Ministry of Finance and Public Credit
VANESSA RUBIO MÁRQUEZ Deputy-Secretary of Finance and Public Credit	ALBERTO TORRES GARCÍA Head of Public Credit Unit Ministry of Finance and Public Credit
ILDEFONSO GUAJARDO VILLARREAL Minister of Economy	ALEJANDRO DELGADO ANAYA President of the Entrepreneur National Institute
PEDRO JOAQUÍN COLDWELL Minister of Energy	VICTOR HUGO LUQUE SALCEDO General Director of Restructuring and Supervision of Companies and State Organizations in the Electric Sector Ministry of Energy
JESUS ALAN ELIZONDO FLORES Financial System Affairs Director at Bank of Mexico	RAÚL JOEL OROZCO LÓPEZ Financial Intermediaries of Development Director at Bank of Mexico
ENRIQUE CABRERO MENDOZA General Director Mexican Council for Science and Technology	ÓSCAR ERNESTO VELA TREVIÑO Head of Insurance, Pensions and Social Security Unit Ministry of Finance and Public Credit
BOARD MEMBERS SERIES "B"	
HOLDERS	DEPUTIES
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MANUEL JESÚS HERRERA VEGA President of the Industrial Chambers Confederation of the United Mexican States (CONCAMIN)	ENRIQUE GUILLÉN MONDRAGÓN National President of the National Chamber of Transformation Industries (CANACINTRA)
ENRIQUE SOLANA SENTÍES President of the Confederation of National Chambers of Commerce, Service and Tourism (CONCANACO-SERVYTUR)	GUSTAVO ADOLFO DE HOYOS WALTHER President of the Mexican Employers' Confederation (COPARMEX)



INDEPENDENT BOARD MEMBERS SERIES "B"

THERE ARE ONLY INDEPENDENT HOLDERS BOARD MEMBERS

CARLOS JOSÉ GARCÍA MORENO ELIZONDO
CFO, América Móvil, SAB de CV

JOSÉ SALVADOR MARTÍNEZ CERVANTES, CPA
Independent Professional

STATUTORY AUDITORS

HOLDERS

DEPUTIES

SERIES "A"

FERNANDO HEFTYE ETIENNE
Delegate and Public Statutory Auditor of Finance Sector
Ministry of Public Function

BRIGITTE CORNEJO JIMÉNEZ, CPA
Sub-delegate and Deputy Public Statutory Auditor of Finance
Sector Ministry of Public Function

SERIES "B"

ARACELI ESPINOSA ELGUERA
Professor and Researcher of Administration and Business
Academic Division, Autonomous Technological Institute of Mexico
(ITAM)

IGNACIO NÚÑEZ ANTA
Comptroller and Manager of Anáhuac Financial Group

BOARD OF DIRECTORS SECRETARY

LÁZARO JIMÉNEZ GARCÍA
Board of Directors Secretary

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



OFFICIALS ATTENDING SESSIONS OF THE BOARD OF DIRECTORS AS OF DECEMBER 31, 2017

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

EDUARDO CALDERÓN CUEVAS

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 LOANTE

Deputy Secretary of the Board of Directors



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MESSAGE FROM THE GENERAL DIRECTOR (CEO)

During 2017, the positive results achieved by Nacional Financiera (Nafin) in support of Mexican companies reflect the effort and commitment of all of us who work in this institution.

Throughout this year, we reached our previously-set objectives, by being constant and consistent and we maintained this course with a policy based on innovation in products and services as well as in the continuous improvement of the traditional ones. We also expanded our actions to increase our presence internationally.

In 2017, we based our efforts on six action lines or axis: Growth, Disruption, Projection, Recognition, Scope, Equality and Responsibility.

In the Growth axis, the private sector portfolio as of December 2017 was MXN 474.490 billion -which includes Financiera Nacional de Desarrollo Agropecuario, Rural, Forestal y Pesquero (National Development Finance for Agriculture and Livestock, Forestry and Fisheries) and the Funds Risk Capital Fund- representing a nominal growth of 105.1% compared to December 2012 and 4.9% compared to the same date in 2016.

The past-due loans percentage stood at 0.88% and the ratio of reserves to total portfolio at 1.98%. Stockholders' equity presented sustained growth to settle at



MXN 31.444 billion as of December 2017, representing a nominal increase of 60% during this administration. Capitalization stood at 14.5%, including the effect of capital injection received last December.

At Nafin, we focused on mitigating barriers on financing SMEs (rates and collaterals), to provide more credits under better conditions. This is how 95% of loans are directed to MSMEs, with an average amount of MXN 1.4 million under three-year terms. By the end of 2017, there were already 61 financial intermediaries, 17 of them added during this Administration.

Nafin sector-based programs attend to public policy guidelines of the Federal Government. The balance in 2017 was MXN 23.896 billion, 40% higher than in 2012 and 26% higher than in 2016.

In regard to the Disruption area, it is important to highlight that, since our return to international markets in 2015, at Nafin we have continued to strategically increase our participation in these markets. Thus, in 2017, two bonds were issued in the Japanese market, for a term of five years, for 10 and 15 billion yen, respectively.

We also placed the First Social Bond issued by a Mexican development bank and listed on the Mexican Stock Exchange, positioning us once again as a leading institution in the promotion of novel instruments.

In compliance with the Financial Reform, Nafin has carried out the development of new products and sector-based programs in support of SMEs, such as Credit for Young People (Crédito Joven), Women Entrepreneurs (Mujeres Empresarias) and the Come to Eat (Ven a Comer) Program, whose results exceeded initial expectations.

One of 2017 initiatives with promising results for training successful entrepreneurs is “Pioneering Minds” (Mentes Pioneras), which seeks to identify entrepreneurial talent in young people at an early age, in order to enhance their abilities. Based on Gallup experience, we designed a test that allows measuring entrepreneurial profiles of a person in 10 areas considered essential for the creation and development of large businesses. It should be noted, as a relevant finding, that young Mexican people resulted with evaluations well above the average produced by other

developed countries where this test has been applied. This motivates Nafin to continue working with programs for youths, since we are the only nation in Latin America applying this type of project.

In the Projection axis, we have further strengthened our cooperation with international financial organizations to take advantage of their experience in areas of common interest and priority for Mexico’s development. Thus, in 2017 we carried out various collaboration agreements with institutions such as the European Investment Bank, Spanish Development Financing Company, Latin American Association of Development Financing Institutions (Alide) and Official Credit Institute of Spain, among others.

Likewise, with the reopening of our London Branch, the strategy to position Nafin within the international financial community is strengthened, since it will facilitate the diffusion of Nafin businesses, projects and services, through the consolidation and diversification of our client portfolio.

Also, this year we presented the Nafin business model and operation, in a comprehensive manner, to other development banks, financial institutions and, in general, public and private organizations, through the third issuance of the International Program on Best Practices for Development Banking: The Nafin Model.

All of these achievements were recognized in September 2017, when I assumed the Presidency of Alide. As General Director of Nafin, I am honored with this distinction and I have taken up the challenge with the support of those who, every day, make the operation of this great institution possible.

Nafin's work, professionalism and leadership as a development bank has earned it important domestic and international awards, such as the Morningstar Award for Best Operator, granted to the Nafin Investment Fund Operator; the recognition for the Verification of Obligations of Transparency-INAÍ, and a sustained recognition of all rating agencies, among others.

Within the Scope axis, our three mobile offices visited Mexico's 32 states, bringing financing and training to small and medium-sized companies. With face-to-face and online courses, we have trained 100,000 beneficiaries a year, on average.

Regarding Corporate Governance, Nafin carried out the 9th Workshop, in Merida, Yucatan; the 10th Workshop, in Mexico City, focused on Future Generations, and the 11th Workshop, in Mexico City, which addressed Non-Banking Financial Intermediaries.

Because equality is fundamental for Nafin growth, we incorporated gender equality in our products and services and increased the number of female advisors in the Nafin Advisory Councils. In 2012 there were only 24 and currently there are 100. Regarding our organizational structure, the number of women in middle and upper management has increased by 43%. Nafin also joined the HeForShe Initiative of UN Women, with a series of commitments to achieve gender equality.

In the Responsibility axis, as a development bank, we are called to lead reconstruction processes and financing in the zones and sectors most affected by weather events and natural disasters. For this reason, in 2017, we started a trust to help people affected by the September earthquakes.

Similarly, we strive to participate in green markets and projects, not only because they are, without a doubt, very profitable, but because we contribute to commitments that Mexico has acquired worldwide in reducing emissions into the atmosphere and, in this way, we work for a better planet for all.

We begin a difficult year in 2017, with adverse economic prospects for Mexico. However, we firmly continue with our strategic commitment of proceeding forward, in a counter-cyclical and innovative way. We approach new sectors of the population and adjust to their needs to provide new services with quality and care for women and young entrepreneurs.

We achieve goals and we have obtained good results to date. This is how we reaffirm our commitment to continue operating Nafin in an effective and efficient manner in 2018, thus strengthening our mission to contribute to the economic and social development of Mexico. ¶

Jacques Rogozinski S.
General Director (CEO)



ECONOMIC ENVIRONMENT

At 2017 end, the world economy grew 3.7%, according to figures from the International Monetary Fund (IMF). This advance would be 0.3% higher than that projected at year's beginning and greater than 0.5% to that registered in 2016. It would also be the first time since 2009 that observed data exceed expectations.

Economic rebound was widespread, after a long episode of heterogeneous growth between regions was observed after the crisis. Developed economies would present the biggest difference since 2017 when they grew together 2.3%, compared to 1.7% in 2016. By countries and regions, the United States grew 2.3% in 2017 against 1.5% in 2016. Euro Zone would have grown 2.4% vs. 1.8%. Japan 1.8% vs. 0.9%, Canada 3% vs. 1.4% and only the United Kingdom grew less than the previous year to advance 1.8% vs. 1.9%.

Emerging and developing economies advanced 4.7%, making initial expectations valid and exceeding 4.4% reached in 2016. Among the countries that presented higher growth rates than 2016 are: China, 6.9% vs. 6.7%; Russia, 1.5% vs. -0.2%; Brazil, 1.1% vs. -3.5%, and South Africa 0.9% vs. 0.3%. By growing 6.7%, India continued to present one of the highest growth rates among large emerging economies; however,



this would have been lower than in 2016, which stood at 7.1%.

The arrival of Donald Trump as president of the United States marked a change in the style of government of that country. In order to comply with its campaign promises, he issued a series of decrees on various matters and sent several initiatives to Congress, of which only the one related to tax reform was approved before 2017 end. This reform has as a fundamental axis the reduction of corporate tax rates from 35% to 21%, as well as lower tax burden on families for 10 years, but with expiration of some provisions from 2025. Although it is expected that with these measures their economy will gain new momentum, they

would also generate an increase in fiscal deficit of around 1.5 trillion dollars that would have to be covered with a higher level of indebtedness.

In the United States, factors that support household spending continued to advance, non-farm payrolls grew by 2.17 million places, hourly wages advanced at an average annual real rate of 0.4%, consumer credit increased by 196 billion dollars, housing prices rose more than 6% and Standard & Poor's 500 index (S&P 500) grew 17.1%.

It is convenient to stop at labor market behavior. Since October 2010, non-agricultural payroll has grown uninterruptedly, accumulating since then 17,245,000 new places, reaching a historical maximum of 147,610,000 jobs at 2017 end. Likewise, unemployment rates closed the period in 4.1% of Economically Active Population (EAP), decreasing by 0.6% in relation to that recorded at 2016 end and placing its lowest level since 2000. It is necessary to point out that these figures would indicate that the economy continues to rapidly approach its full employment level, with which price pressures from demand become more likely.

Consumer inflation measured by Personal Consumption Expenditure (PCE) deflator, which is an indicator for which the Federal Reserve System (Fed) has an annual variation target of 2%, exceeded in January and February that level to decelerate again at the end of the year at 1.7%, 0.1% below 2016 close level. In the case of an index that does not consider energy or food prices, although it maintained an upward trend between March 2016 and February 2017, it never exceeded the 2% level and, between March and June 2017, it presented a downward trend that led it to an annual variation of 1.5% at 2017 end, which meant a reduction of 0.4%.

Under these circumstances of moderate growth, low unemployment and absence of inflationary pressures, the Federal Reserve continued with a process of normalizing its monetary policy by increasing its reference rate in March, June and December, by 25 basis points (bp) each time, raising the ceiling of its range to 1.50%. Also, at its meeting in June, it announced some program principles to reduce its balance, which began in the last quarter 2017.

In other countries and regions of the world, unemployment rates and inflation showed a behavior similar to that observed in the United States. In the Euro Zone, for example, unemployment rates in December reached 8.7% of EAP, which is its lowest level since February 2009 and a year-end since 2008. Inflation closed at 1.4%, after having reached 2% in February, a figure that was not observed since January 2013. In terms of core inflation, although reached 1.3% in March, it ended 2017 at 0.9%, the same level of closure since 2015.

The economy of the United Kingdom surprised by its resistance to Brexit, although it would have grown less than in 2016, did not have a significant slowdown. Inflation in the region reached 3% at 2017 end, being the highest level for a full year since 2011. Regarding unemployment rates, until November stood at 4.3% of EAP, and although this is not year-end data, it is necessary to point out that the lowest unemployment rate for a full year before that in 1974 with a level of 3.7%.

Japan, despite a better growth, a reduction of unemployment rate to 2.7% of EAP (lower level for a full year since 1992, 2.3%) and continuous fiscal and monetary stimulus measures, has not

been able to boost inflation at sustainable levels far from zero. In 2017 prices grew at an annual rate of 1% and core inflation was only 0.3%.

Finally, in Canada, unemployment rates fell to 5.8% in 2017, with its lowest level for a full year since this indicator began to be published in 1976. In terms of consumer inflation, 2017 ended at 1.9%, the highest since 2011, while the underlying component of the price index had an annual variation of 1.6%, which is the same level since 2012.

Central banks of these countries and regions made different decisions. The European Central Bank (ECB) did not move its rate and noted that, at some point, probably from the fourth quarter of 2018 could begin to reduce its asset purchase program. The Bank of England increased its rate to 0.50%, from 0.25% to the one that had fallen after Brexit. The Bank of Canada, finally, raised its benchmark rate by 50 bp, 25 bp at its mid-July meeting and an additional 25 bp in September to bring it to 1%.

Mexican Economy

In 2017, with preliminary data for the fourth quarter, the Mexican economy grew 2.1%. Although this advance was lower than the one observed in 2016 of 2.3%, it exceeded expectations at year's beginning that predicted a growth of just over 1%. External threats at year's beginning were gradually diluted. An exit of the North American Free Trade Agreement (NAFTA) became a renegotiation, border adjustment taxes were eliminated from tax reform. There was no mass expulsion of Mexican migrants. Foreign Direct Investment (FDI) was not stopped and portfolio investment continued to enter.

Considering the demand side, Mexican economy continued to be driven by private consumption, which up to the third quarter had an average advance of 3.1%, although towards year's end some deceleration began to be observed.

Total investment contracted -1.3% for the same period, while private investment contracted -0.2% and public investment -7.6%. Investment in construction has not been able to recover, but investment in machinery and equipment has. Exports showed greater dynamism, growing by 4.3%, after being at 2.8% in the same period of 2016.

More recent figures indicate that during October-November 2017, Global Indicator of Economic Activity (IGAE) registered an annual growth of 1.5%.

Among other indicators of aggregate demand, we can mention that sales of the National Association of Self-Service and Departmental Stores (ANTAD) expanded at a real annual rate of 0.9% during 2017's last quarter. Likewise, during October-November 2017, wholesale commercial activity had an annual increase of 1.4%, while retail activity decreased at an annual rate of 0.8%.

As for investment, in October an annual decrease of -2.6% was observed. Domestically, investment in construction had an annual reduction of 4%, while investment in machinery and equipment fell 0.9%.

Foreign sector continued to grow in the fourth quarter, with an increase in total exports of 10.1% measured in dollars at nominal value. Oil exports increased at an annual rate of 35.1%, while agricultural, extractive and manufactures exports grew at annual rates of 12.7%, 10.8% and 8.4%, respectively. Within

manufacturing exports there was an annual increase in automotive and non-automotive sectors of 13.2% and 6%, respectively. In turn, imports had an annual expansion of 11%.

Formal employment continued to strengthen. The number of insured persons to the Mexican Social Security Institute (IMSS) of an urban nature, both permanent and temporary, as well as permanent agricultural jobs, closed the year at 19,184,191, which meant an increase of 779,803 workers. This is the largest number of jobs created in the history of Mexico in a year. Likewise, the total number of jobs generated in a 6-year period totaled 3,282,359, which is also the largest number of formal jobs created in any 6-year period. Wages also continued to advance. Wages to workers registered at IMSS grew 4.81% on average during 2017. However, an increase in inflation reduced ex-post real wages by 2.14% after 2015 and 2016 registered an average advance of 1.51% in purchasing power. Finally, unemployment rate stood at 3.13%, being the lowest for a calendar year since 2005. It should be noted that despite an increase in formal employment, informality rate was 56.7% at 2017 end, which meant a reduction of only 0.06 in relation to that observed in December 2016.

Other positive data for the Mexican economy were family remittances sent from abroad, which showed a record high of 28.771 billion dollars.

Mexico, the United States and Canada entered into a process of modernization of NAFTA, after Donald Trump threatened to abandon because he considered it unfair to his country. Between August and December, five

rounds of negotiation took place, from which significant advances were obtained in terms of SMEs, telecommunications, competition policy, digital commerce, good regulatory practices, and customs and commercial facilitation, among other areas. Issues where positions have been found as rules of origin, dispute resolution mechanisms and five-year termination clause were pending.

In terms of inflation, an increase of more than 20% in gasoline in January, accumulated depreciation of Mexican peso since July 2014, temporary increase of some agricultural products in the first half of 2017 and the increase of close to 30% of LP gas in the second semester along with a new outbreak of depreciation in the last months of 2017, caused annual inflation to end at 6.77%, this being its highest level for a full year since 2000 when it reached 8.96%. Core inflation ended at 4.87%, being in this case the highest since 2008 when it was 5.54%.

In 2017, prices of processed foods advanced 6.82%, while those of non-food merchandise increased by 5.62% and services by 3.76%. Energy prices rose 17.7%.

The Bank of Mexico (Banxico), in order to contain medium-term expectations and contribute to maintaining the solidity of macroeconomic fundamentals raised its reference rate by 125 bp, bringing it to the level of 7% in the first half of 2017. From there, it made a prolonged pause to reapply a new increase of 25 bp in December, with which in 2017 the funding rate ended at 7.25%, its highest level since March 2009.

Finally, regarding Public Finances, Public Sector Financial Requirements (RFSP) registered a deficit equivalent to 1.1% of Gross Domestic

Product (GDP), an amount that was lower than that observed in 2016 of 2.8% of GDP, as well as the goal of 2.9% of GDP presented in General Economic Policy Criteria for 2017. When excluding resources from Banxico Operating Remainder (ROBM), RFSPs in 2017 were located in a deficit of 2.6% of GDP, also below the level observed in 2016 and the target for 2017.

Fiscal discipline, ROBM, appreciation of peso, adequate management of public debt and increase in nominal GDP, both due to higher inflation and a change in measurement methodology, resulted in Historical Balance

of Financial Requirements of Public Sector (SHRFSP) at the end of 2017 was 46.2% of GDP, lower than 48.7% at 2016 end, and for the first time in 10 years, the whole Public-Sector debt as a percentage of GDP decreased.

After an intense appreciation of pesos against dollars of 11.9%, going from \$20.62 at the end of 2016 to \$18.16 at the end of September, between October and December the peso-dollar exchange rate increased 8.3%, when it reached \$19.66 at the end of the 2017 activity. In the year, the Mexican peso gained 4.6% against the U.S. dollar. ¶

PROMOTION

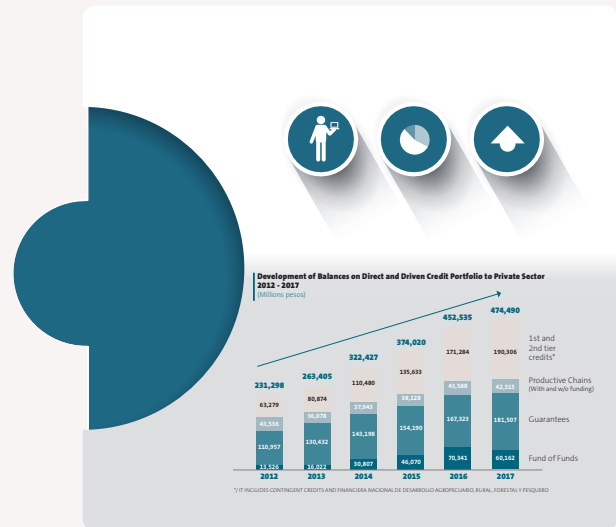
Promotion Program

Nafin, through its different credit and guarantee programs, channeled resources in 2017 for 550.834 billion pesos, of which 56.9% corresponded to Second Floor loans; 40.1%, to loans through Guarantees Programs and 2.2% of private first floor operations, and 0.8% to operations with the Mexican Development Bank (Financiera Nacional de Desarrollo Agropecuario, Rural, Forestal y Pesquero).

Credit and Guarantees to Private Sector Program

The variety of products offered by Nafin through its programs of Productive Chains, Traditional Discount, Micro Business and Equipment, as well as our Guarantee Scheme itself and credits guaranteed by the latter, allowed channeling resources to the private sector for 546.534 billion pesos, which made it possible to support 565,531 beneficiaries, including 158,788 companies and 406,743 microcredits. Of all beneficiaries, 99.8% were micro, small and medium business.

Through Second Floor operations, resources were channeled for a total of 313.874 billion pesos, Productive Chains participated with a grant of credit for 194.318



billion pesos, Micro Business and Equipment with 34.235 billion pesos and Traditional Discount with 85.321 billion pesos.

Our Guarantee Program encourages the granting of credits to SMEs, since Nafin participates in the risk on financing granted by Financial Intermediaries (FI). From January to December 2017, 220.696 billion pesos were channeled (including guarantee financing and guaranteed credits). In this way, considering guaranteed credits, the balance is at the end of the period at 181.507 billion pesos, 8.5% higher than at the end of December 2016. From this balance, there is a coverage of Nafin Guarantee of 40%.

Productive Chains Program

By 2017 end, through our Productive Chain Program 194.318 billion pesos were granted, which generated a balance of 42.515 billion pesos. Within this program, during 2017 Federal Government agencies registered accounts payable for 310.947 billion pesos, of which 29% was charged in advance. This allowed to support 4336 suppliers that exercised the benefit of early collection through financial factoring.

During 2017, the Program's main indicators are the following:

- More than 450 First Order Companies (EPO) with operations, benefiting more than 21 thousand suppliers.
- More than 2.3 million documents were operated.

Promotion activities continued to be developed to register, during 2017, a total of 40 new chains and 296 in promotion and implementation phases.

The Program's main results, with respect to the same period of 2016, are the following:

- Operation of suppliers in private sector companies increased to 5.148 billion pesos, equivalent to 4%.
- Balance in private sector companies grew 761 million pesos, which is equivalent to 3%.
- Operation rate against the entire Program increased from 43% to 45%.

Sector-based Programs

Nafin offers programs to assist MSMEs in sectors or economic activities that have seen their access to financing limited, as well as

programs to promote job creation and support strategic or priority sectors. At the end of 2017, these programs have reached a historical balance of 23.896 billion pesos, which implied a growth of 26% compared to 2016. During 2017, 20,483 loans were granted, for 17.182 billion pesos.¹ By line of action, the main results were the following:

I. Financial Inclusion. 8700 credits were granted for 6.238 billion pesos, highlighting the following:

- » **Support Program for Women Entrepreneurs:** incorporates a gender perspective in credits to MSMEs, to promote competitiveness and growth of businesses run by women in Mexico. 4188 loans were granted for 4.718 billion pesos.
- » **Credit for Young People Program:** grants credit to young people between 18 and 35 years old who wish to start their business or grow the one they already have. 2723 credits were granted for 1.140 billion pesos.
- » **Program of Financing to Broadcasting Companies:** aimed to finance considerations of concession titles to radio broadcasting companies. The first 22 credits were granted for 133 million pesos.

II. Regional Development. 2093 credits have been granted for 3.539 billion pesos, which mainly include the following programs:

¹ The amounts of credit granted in Sector-based Programs consider the amount of authorized credits.

- » **Programs of Economic Impulse and Promotion to Employment:** It operates in coordination with governments of participating states to support their priority economic activities and contribute to regional development and job creation. 1868 credits were granted for 3.264 billion pesos.

State Credits	Granted	Amount Placed (Million Pesos)
Oaxaca	431	700
Nuevo León	212	454
Chiapas*	184	306
Jalisco	151	278
Michoacán*	115	189
Aguascalientes	112	182
San Luis Potosí	74	157
Sonora	89	157
Querétaro	103	156
Sinaloa	100	146
Zacatecas	72	124
Hidalgo	41	114
Guanajuato	85	111
México	34	90
Durango	20	37
Guerrero*	17	28
Tamaulipas	20	26
Yucatán	7	8
Puebla	1	1
Total	1,868	3,264

*Under the South East Program, Aligned to Special Economic Zone strategies.

It should be noted that during 2017, operations began under this scheme with the Mexican states of Durango, Hidalgo and Querétaro. Likewise, extensions of portfolio were made in Aguascalientes, Jalisco, Nuevo León, Sinaloa and Zacatecas.

- » **Economic Boost Program for Financing in Border Areas:** It supports with financing under competitive conditions companies of states located in the North and South borders of Mexico: Baja California, Baja California Sur, Sonora, Chihuahua, Tamaulipas, Coahuila and Quintana Roo. 127 credits were granted for 161 million pesos.

III. Providers Development. 1747 credits were granted for 3454 million pesos, highlighting the following:

- » **Support Program for Construction Sector:** It supports companies in this sector dedicated to the development of commercial infrastructure. 1380 credits were granted for 2664 million pesos.
- » **Support Program for Leather and Footwear Sectors and its Supply Chain:** It supports the productive chain of leather and footwear sectors with financing to promote technological development, operational and administrative modernization. 224 credits were granted for 353 million pesos.

IV. Modernization and Equipment. 1757 credits were granted for 3225 million pesos.

- » **Automotive Industry:** It supports renovation of cargo, passenger and tourism vehicle fleets. 697 credits were granted for 1.730 billion pesos.
- » **Come to Eat Program:** Financing directed to restaurant companies

for working capital, equipment and modernization of facilities. 512 credits were granted for an amount of 795 million pesos.

- » **Gasoline Companies Program:** It supports gas station companies with financing to make necessary investments for their modernization, facing new conditions of competition in the energy industry. The first 65 credits were granted for 162 million pesos.

V. Economic Reactivation. 576 credits were granted for 667 million pesos:

- » **Financing Program for Economic Reactivation of Campeche and Tabasco:** It was implemented as part of a series of measures of the Federal Government and governments of both states to counteract the impact of the fall in oil prices in their economies. 292 credits were granted for 298 million pesos.
- » **Support Program for Companies Affected by Earthquakes:** Given the earthquakes on September 7 and 19, a program was launched to contribute to the recovery of affected areas, through financing to MSMEs and individuals with business activity, to make investments that they require with the purpose of restoring their productive capacity and preserving sources of employment. 284 loans were granted for 369 million pesos in Mexico City, Chiapas, Morelos and Oaxaca.

VI. Sustainable Financing. 5869 credits were granted for 340 million pesos.

- » **Through the Energy Efficiency Program “Eco Business Credit Program”,** in its *massive* and *individualized* modalities, micro and small companies are supported for the acquisition and/or substitution of efficient equipment that generate a saving of electricity. 5783 credits were granted for 338 million pesos.

Promotion of Sector-based Programs

Develops and implements promotion and sales strategies of some Sectoral Programs through Nafin’s Promoters Network, highlighting the Economic, Emerging and those programs designed to strengthen some economic sector, such as Young People Credit, Women Entrepreneurs, Leather and Footwear, Financing to Higher Education, Come to Eat Program and Stimulus to Good Taxpayers.

In 2017, Sectoral Development Indicators had a greater efficiency to SMEs in the above-mentioned programs, obtaining the following results in the year:

- 92% of SMEs are attended in five business days (from assignment of cases).
- Once a SME confirms its interest in financing, 90% of files are integrated within 10 business days.
- 93% of integrated files are sent to a financial intermediary window within a period not exceeding five calendar days.

Factoring Promotion

Generates and implements strategies of promotion and affiliation to Factoring Programs

in Productive Chains and Supplier Financing, in conjunction with clients of Alternate Channels Division, using our Promoters Network and various means such as: telephone campaigns via Service Center to Clients, emails, events and information modules, among others.

Main results of 2017:

- Affiliation of 4040 new suppliers to Productive Chain Programs.
- 94% of suppliers that had publication registered operations.

Electronic Products Administration

It controls Administration and Document Management platforms, as well as Nafinet, a platform in which products from Productive Chains, Distributor Financing and Electronic Credit are electronically operated, as well as training, specialized advice and technical support are provided to FIs, EPOs and internal areas. Likewise, it carries out documentary reviews of affiliation files to Productive Chains and of certain sector-based programs.

Some of this platform volumes include:

- Supervision and monitoring of more than 9400 daily operations on average (Chains and Credit at Fixed, Variable, Emerging and Microcredit Rates) with average amounts of more than 1.047 billion pesos per day.
- Attention and support to more than 67 banking and non-banking financial intermediaries for credit operations and consultations.
- Dispersion of funds to SMEs and financial intermediaries, with an average of 800 million pesos per month on account of EPOs through Productive Chains.
- Implementation of 22 productive chains.

Customer Service and Channel Development

Contracts and manages our Customer Service Center and Trust Fund 80444 “Technical Assistance Fund for Financing Programs”, through which Sectoral Promotion and Factoring areas have resources for the implementation of promotion and attention strategies of different programs.

The main results of 2017 are:

- Attention to 235,533 telephone calls, of which 83% correspond to users of Productive Chain Programs.
- Suppliers of Productive Chains made discounts of their invoices by telephone for 25.533 billion pesos, which represents 11% of the total operated amount in this Program.
- Through our Entrepreneur Support Network, 5425 applications were attended, of which 29% require training services and 71% financing.

Entrepreneurial Capital

Promotes investment in projects directly or indirectly through investment funds. It is composed of six portfolios: Conacyt-Nafin Fund, Seed Capital Co-Investment Fund, Inadem-Nafin Entrepreneur Capital Ecosystem, Crowdfunding Project, Mexico-Ventures Fund and IMPI-FUMEC Patent Support Program. These are managed and operated through participation in Boards of Directors and Assemblies of Shareholders of certain Companies, Investment Committees of Funds and follow-up meetings with Contributing Bodies.

The main results obtained are:

- **Conacyt-Nafin Fund.** The total investment of this program was 224 million pesos in 43 companies, currently in a disinvestment

phase. Disinvestment has been negotiated in 14 companies for an amount of 75 million pesos.

- **Seed Capital Co-Investment Fund.** Capital has been committed for 346 million pesos in seven investment funds, which have supported 74 companies, 16 of which received direct support for 79 million pesos with two successful outputs. During 2017, the most relevant operations were:
 - » Formalization of Soldiers Field Angels Fund for 40 million pesos.
 - » Nine funds were reviewed, from which the following funds were approved: Redwood Ventures Fund I, Leap Partners I, Alacrity Fund and Dila Capital III, which have resources contributed by governments of Mexico City and Jalisco and the Ministry of Economy.
 - » Reuse of resources from disinvestments and interest generated was authorized as investments are made for new projects.
- **Inadem-Nafin Entrepreneur Capital Ecosystem.** It is estimated that the total amount of this Program is 5.629 billion pesos (public and private resources) with a participation of an Entrepreneur Capital Trust of 2.055 billion pesos to support 39 investment funds, which have invested in 157 companies. Of these 39 funds, in 2017 five funds were formalized, from the 2016 call, the Supply Capital Fund to invest in projects of Federal Government suppliers and Pacific Alliance Fund for investment in companies in Mexico, Colombia, Chile and Peru. Likewise, Entrepreneur Capital

Trust formalized its collaboration as a broker body in the 2017 Call.

- **Mexico Ventures Fund.** There are four funds in operation with resources of 475 million pesos.
- **IMPI-Fumec-Nafin Patent Support Program.** In 2017, we participated in the Second Innovation Conference of IMPI-Fumec-Nafin Patent Support Program, that addressed issues related to Financing Mechanisms for Technology and Industry-Based Projects 4.0. In this program, resources are available for 17 million pesos.
- **Crowdfunding Project.** It was defined that with the remaining 107,000 dollars of the initial contribution of Nafin (200,000 dollars), the second stage of the Crowdfunding Industry Diagnosis will be carried out, which includes the analysis of new platforms, technical assistance to the ones already existing and is done in conjunction with Association of Collective Funding Platforms (Afico), Multilateral Investment Fund of Inter-American Development Bank (IDB-MIF) and the Entrepreneur National Institute (Inadem).

Alternative Channels

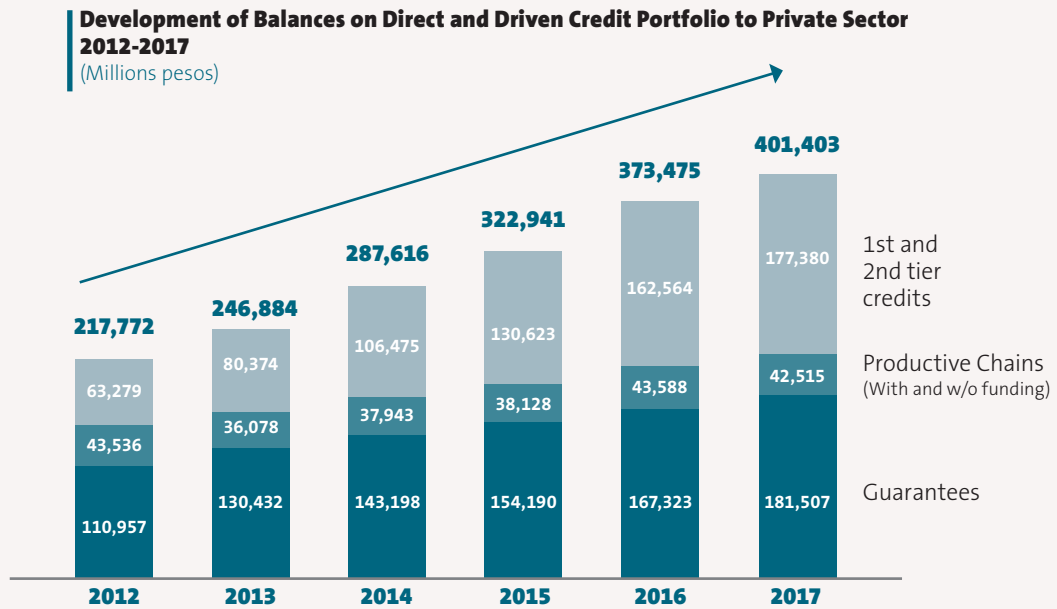
Provides advice to MSMEs and entrepreneurs, through our Customer Service Center and Promoters Network, in the process of affiliation of suppliers to Productive Chains Program and to obtain sectoral financing. It also provides training, technical support and specialized advice for the operation of electronic products to EPOs and FI. Additionally, it develops entrepreneurial capital markets through

investment in innovation projects and high impact through both investment funds and directly.

Portfolio Balances for the Private Sector Credit

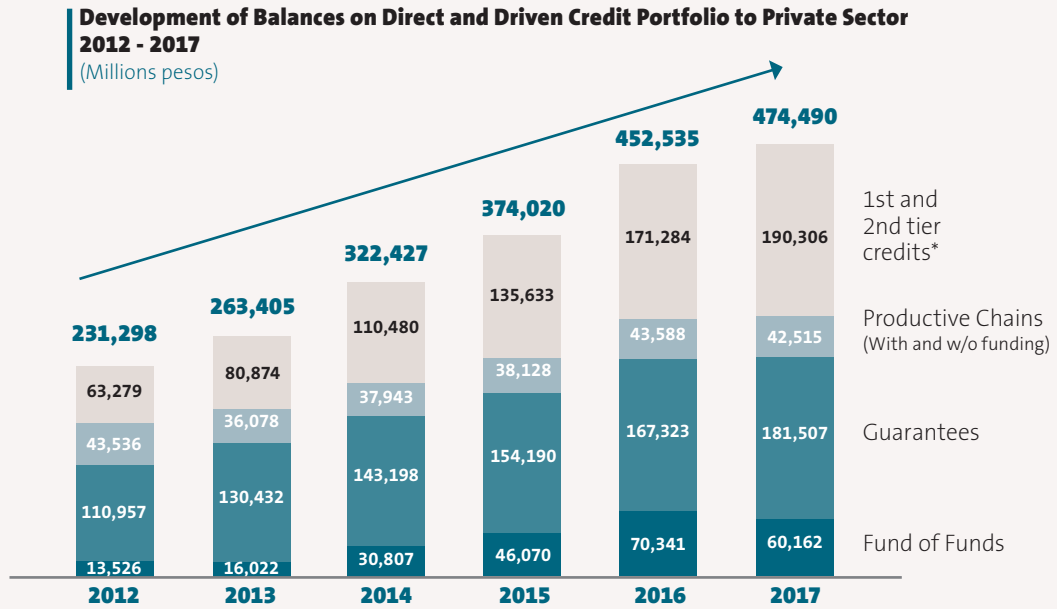
Our balance of total credit portfolio to private sector, including guaranteed credits, at the end of December 2017 is increasing with

an amount of 401.403 billion pesos, which represents an increase of 27.928 billion pesos (7.5%) with respect to last year's same period. From this amount, Guarantees Program contributes with 45%, traditional credits with 44% and Productive Chains with the remaining 11%. In accordance with its mission to support very small companies in Mexico, 76% of portfolio balance to private sector was concentrated in MSMEs.



Balance of Private Sector Portfolio, including Financiera Nacional de Desarrollo Agropecuario, Rural, Forestal y Pesquero and

the Fund of Funds, was at 2017 end at 474.490 billion pesos. Compared to December of the previous year, this balance increased 4.9%.



*/ IT INCLUDES CONTINGENT CREDITS AND FINANCIERA NACIONAL DE DESARROLLO AGROPECUARIO, RURAL, FORESTAL Y PESQUERO

Business Training and Technical Assistance Program

From January to December 2017, with our Training, Technical Assistance and Internships Program, 142,020 entrepreneurs and/or MSME entrepreneurs benefited from courses taught at Business Development Center (CEDEM), mobile offices, our Consultants Network, workshops, conferences, e-learning platform and internships.

Beneficiaries

	2017 Annual Program	Jan-Dec 17 Realized	Advance (%)
Trained Totals:	109,500	142,020	130
Face to face	49,800	62,484	125
Online*	52,500	60,349	115
Mobile Office	7,200	19,187	266

*Accumulated

In addition to its financial activity, based on its Training and Technical Assistance Program strategies, at 2017 end, Nafin carried out the actions detailed below:

- In CEDEM's new facilities various services have been granted for the benefit of SMEs (linkage, conferences, etc.).
- In 2016, the "Diagnostic for Micro and Small Businesses" course was implemented in our online platform, whose main objective is to define more precisely training and technical assistance needs of micro and small companies, thus strengthening their areas of opportunity based on administrative processes. As of December 2017, 4087 companies and entrepreneurs have been self-diagnosed.
- New training content was added for MSMEs, including online courses such as "Human capital is at SME's heart",

"Determine your costs well", "Quality for MSMEs", "How to make my family business an institutional enterprise", "Building socially responsible companies" and "Learn to borrow", in order to make current issues available to beneficiaries to improve their administrative process.

- Online courses such as "Products and services for your company", "SME products and services for promoters" and "20 steps to start or improve your restaurant" were updated.
- As for Corporate Governance (CG), the 9th workshop was held in Mérida, on May 24-26, 2017, with an attendance of 61 people and 24 companies, and an acceptance of 92%. Likewise, our 10th workshop was held in Mexico City on November 22, 2017, focused on Future Generations, with an attendance of 37 people and 15 companies and 93% acceptance and, finally, our 11th workshop was held in Mexico City on November 8, 2017, focused on Non-Banking Financial Intermediaries (NBFIs), with an attendance of 59 people and 29 NBFIs and an acceptance of 94%.
- Since the beginning of our Training and Technical Assistance Program, on CG axis, 292 companies and 703 entrepreneurs have been supported through 11 CG workshops. It also supported 368 entrepreneurs who attended the Magna Conference "Corporate Governance in Family Business".
- In the same axis, with the Development Bank in Latin America (CAF), and the Foundation for Sustainable Development in Mexico (Fundes), a pilot project for CG in Mexican family businesses was

implemented, thanks to which 16 companies started their protocol process in 2017.

- Nine internships with the World Bank were carried out: Technical support to institutions that seek to improve entrepreneurship services; business incubators and innovation in employment and vocational education sectors for young people in Guatemala; Foreign Trade Investment Bank (BICE); Universidad Veracruzana and Higher Technological Institute of Xalapa; Autonomous University of Sinaloa; Tecnológico de Monterrey, State of Mexico Campus; Mexican Institute of Finance Executives (IMEF), and the Third International Program of Best Practices for Development Banking: Nafinsa Model, which had 46 participants, 33 external (representatives of 17 international institutions from 15 countries) and 13 internal, with a level of satisfaction of 94%.
- In the field of Energy Efficiency (EE) in SMEs, in June the workshop “How to improve the energy efficiency of your SME” was carried out, in collaboration with Engineering Faculty of UNAM, whose objective was to sensitize and invite participants to incorporate EE actions in their companies, obtaining an acceptance of 92%. Likewise, in face-to-face channels, awareness on this topic was reinforced. Also, a webinar was carried out in collaboration with National Commission for the Efficient Use of Energy (Conuee) on December 18, 2017, which had 355 views in 10 countries.
- In July 2017, the Project Evaluation Certification was finalized, whose purpose

was to strengthen institutional capacities in priority projects and programs. This Certification had 21 participants: two from Ministry of Finance and Public Credit (SHCP), one from National Bank of Public Works and Services (Banobras), one from Inadem and 17 from Nafin.

Regarding channels of attention, the following stands out:

- With three Nafin mobile offices, part of Mexico was visited, in such a way that 1151 courses were taught and 19,187 people were trained.
- Through CEDEM and together with a network of 47 instructors nation-wide, 2810 face-to-face courses were taught with which 62,115 people were trained.
- Of this total, 200 face-to-face courses corresponded to Fiscal Incorporation Regime (RIF), with 4157 people trained.

The online platform www.nafintecapacita.com has 32 business development courses and 60,349 active users who have taken a total of 103,176 courses.

Additionally, Nafin participated in several events of the National Week of Financial Education, organized by National Commission for Protection and Defense of Financial Services Users (Condusef) and the Mexican Bank Association (ABM), with the placement of a Mobile Office and delivery of training courses. Ministry of Foreign Affairs (SRE), through the Institute of Mexicans Abroad (IME), invited Nafin to participate in the Sixth Week of Financial Education (SEF) 2017 for the United States and Canada, which took place in March under the motto “Save, invest and

build your estate". It is worth mentioning that Nafin also participated in SEF 2016 edition, with the promotion of our Online Training Program.

In SEF 2017, programs and actions to support Mexican-origin population in the United States, which amounts to 36.9 million people, of which 12.2 million were born in Mexico, were disseminated,² and promote exemplary projects with resources to strengthen them and generate mechanisms for consolidation or, where appropriate, expansion. States with highest concentration of undocumented Mexicans per county are: California, Texas, Arizona, New York, Illinois, Nevada, Colorado, Georgia and Utah.

The proposed participation of Nafin in SEF 2017 focused on providing:

- Information, through a guide on entrepreneurship issues, business management and credit support available in the market and its main characteristics. This document was published as part of a booklet that was in charge of Banco Azteca, at the request of Condusef.
- Promotional banners for dissemination in electronic media aimed at Mexican immigrants, with the aim of publicizing our online training platform www.nafintecapacita.com.

Regional Promotion Network

Credits and guarantees granted to private sector at 2017 end amounted to 546.534 billion pesos, supporting a total of 565,531 beneficiaries,

including 158,788 companies and 406,743 microcredits. Of all beneficiaries, 99.8% were micro, small and medium size companies. By regional classification, the Central region highlights with a participation of 51%.

As a main sales channel for products and services of Nafin in Mexico's 32 states, our Deputy General Directorate of Regional Promotion and Institutional Relations carries out their promotion and assists with administrative areas in their implementation.

Activities of promotion and institutional representation that were developed during 2017 had as objective:

- Disseminate institutional works of Nafin in Mexican states.
- Promote portfolio of products and services that Nafin has for different business segments.
- Establish local alliances for the promotion of institutional products in support of SMEs.
- Capture requirements and needs of business sectors and governments of Mexican states.
- Generate business for Nafin with a focus on regional development.

Results reported by this Deputy General Directorate in favor of regional and sectoral development of Mexico during 2017 were the following:

- Nafin contracts were expanded with more companies, particularly with SMEs, when visiting 1081 new companies of an estimated of 896 to reach a satisfactory goal; that is, there was an achievement of 121%. Through these visits, financing needs were detected and Nafin's offer of products and services was disseminated.

² Undocumented population (DACA and DAPA), subject to deportation.

**Operation for Promotion of Private Sector
By Second-tier, First-tier and Guarantees
Regional Classification**

(Millions of Mexican Pesos - Number of Companies)

Credit and Collateral Jan-Dec 2016			Credit and Collateral Jan-Dec 2017		Percentage Variation 2017/2016	
Amount	Company		Amount	Company	Amount	Company
550,789	715,741	TOTAL	546,534	565,531	(0.8)	(21.0)
29,388	42,990	NORTHWEST	28,882	33,204	(1.7)	(22.8)
9,139	17,393	Baja California	9,165	12,109	0.3	(30.4)
1,783	5,946	Baja California Sur	1,698	1,800	(4.8)	(69.7)
10,721	6,430	Sinaloa	9,742	5,386	(9.1)	(16.2)
7,745	13,221	Sonora	8,277	13,909	6.9	5.2
105,964	108,201	NORTHEAST	100,969	73,473	(4.7)	(32.1)
14,531	17,785	Coahuila	12,662	13,760	(12.9)	(22.6)
11,056	8,376	Chihuahua	10,581	9,373	(4.3)	11.9
3,925	13,421	Durango	3,903	5,274	(0.6)	(60.7)
66,599	39,223	Nuevo León	66,254	27,503	(0.5)	(29.9)
9,853	29,396	Tamaulipas	7,569	17,563	(23.2)	(40.3)
89,181	126,723	CENTER WEST	85,985	108,684	(3.6)	(14.2)
4,831	6,313	Aguascalientes	4,486	3,655	(7.1)	(42.1)
5,241	3,462	Colima	3,122	3,068	(40.4)	(11.4)
14,794	18,007	Guanajuato	16,993	16,139	14.9	(10.4)
41,261	27,987	Jalisco	40,110	28,925	(2.8)	3.4
8,729	30,186	Michoacán	8,091	19,889	(7.3)	(34.1)
1,852	5,133	Nayarit	1,734	3,156	(6.4)	(38.5)
9,378	29,403	San Luis Potosí	8,666	27,669	(7.6)	(5.9)
3,094	6,232	Zacatecas	2,782	6,183	(10.1)	(0.8)
280,679	290,908	CENTER	290,194	223,965	3.4	(23.0)
183,261	88,029	Mexico City	202,803	62,125	10.7	(29.4)
2,946	32,596	Guerrero	2,352	13,174	(20.2)	(59.6)
6,614	14,064	Hidalgo	6,713	16,093	1.5	14.4
52,322	77,039	State of Mexico	51,082	69,367	(2.4)	(10.0)
7,430	19,518	Morelos	3,797	20,059	(48.9)	2.8
8,720	9,220	Querétaro	8,571	6,452	(1.7)	(30.0)
17,894	43,764	Puebla	13,725	29,273	(23.3)	(33.1)
1,492	6,678	Tlaxcala	1,151	7,422	(22.8)	11.1
45,577	146,919	SOUTH-SOUTHEAST	40,504	126,205	(11.1)	(14.1)
5,242	10,078	Campeche	3,248	10,970	(38.0)	8.9
4,516	16,697	Chiapas	4,707	24,517	4.2	46.8
3,053	15,960	Oaxaca	3,096	8,474	1.4	(46.9)
3,594	11,745	Quintana Roo	4,009	16,011	11.6	36.3
5,740	13,877	Tabasco	5,663	6,825	(1.3)	(50.8)
17,329	64,168	Veracruz	13,512	48,685	(22.0)	(24.1)
6,103	14,394	Yucatán	6,269	10,723	2.7	(25.5)

- It helped to position the Nacional Financiera brand in most of the states, through the design of routes followed by our three Nafin mobile offices. Likewise, contact ties with municipal authorities were extended, through the management of corresponding permits for installation of mobile offices and the local promotion of training offers by Nafin in 123 municipalities.
- 20 collaboration agreements were signed with business organizations, education sector as well as state and municipal governments, with the aim of: “Join efforts between ALL PARTIES to provide information and guidance on access to financing micro, small and medium enterprises that are affiliated with [agency] as well as training programs and courses developed by Nafin to be taught either by electronic means and/or in person.”
- Such 20 collaboration agreements were distributed as follows: three in the Central Region (Guerrero, Querétaro and Hidalgo); four in the Northeast Region (Nuevo León, Durango, Coahuila, Tamaulipas); five in the Northwest Region (three in Sonora, one in Baja California and one in Baja California Sur); four in the Western Region (three in Aguascalientes and one in Jalisco), and four in the Southern Region (Oaxaca, Chiapas, Yucatán and Campeche).
- 938 publications and interviews were carried out in local media.
- Network of State Representatives participated as a speaker in 678 promotional events, to disseminate Nafin programs and products to MSMEs.
- As a result of promotion and support

activities, during 2017 an amount of 16.575 billion pesos was placed; that is, 8% more than 2016.

- From that amount, it is highlighted that 34% corresponded to Selective Guarantees and 21% to Sector-based Programs, where State Representatives managed the support of state governments for a better performance in the different regions of Mexico.

Advisory Councils

During 2017, a strategic relationship of Nafin with businessmen throughout the country was strengthened through Advisory Councils, which additionally have become one of the main communication channels between the Federal Government and the business sector.

At present, this citizen-participation network has 660 advisors. Likewise, an increase in the participation of business women in Advisory Councils has been a constant task of gender inclusion, so during 2017 there were 100 women advisors.

Regarding Advisory Councils activity, during the year, 127 sessions were held in all 32 states. It is worth noting the participation of businessmen and directors of Nafin in the five state Work Committees, which focused on strategic issues to maximize their contributions and make their proposals viable. These themes are: Product Design Attending to Regional Vocations, Promotion and Inclusion of New Customers, Support for Entrepreneurs and Promotion of Innovation, Training and Technical Assistance and Institutional Relations.

The five Work Committees functioning in 2017 and dissertations held during plenary sessions of Council contributed to the

generation of 366 agreements related to the promotion of institutional services and generation of business, normally referred to as “business agreements”, of which at the end of December 320 requests were attended, representing an advance of 87%.

2017 report on business agreements by Regional Office:

Regional Office	Agreements Generated 2017	Agreements Delivered 2017	%
Center	87	86	99%
Northeast	54	50	93%
Northwest	40	35	88%
West	107	81	76%
South	78	68	87%
Total	366	320	87%

Advisory Councils have helped Nafin to identify opportunities for programs that promote regional and sectorial economic development, as well as to obtain new strategic clients from the private sector. Likewise, their contribution covered areas of opportunity with the public sector, through participation of each state’s Minister of Economic Development, which have supported collaboration agreements in our five regional divisions. These agreements include joint and coordinated actions for promotion of Nafin products and training and technical assistance programs.

During 2017, advisors referenced various prospects for placement of Nafin products and services, such as: Selective Guarantee, Productive Chains, Treasury Contracts, Credit for Young People, Women’s SMEs, Corporate Financing, Sustainable Projects, Non-Banking Financial Intermediaries and Tailored Sector-based Programs.

In May and November, advisers actively participated in the promotion of the “9th and 10th Corporate Governance Workshop for Family Businesses” that took place in Mérida, Yucatán, and Mexico City, respectively, attended by more than 110 businessmen and in which attendees were made aware of the impact that proper Corporate Governance practices have on companies and businesses and, consequently, in Mexico’s economy, becoming a forum for discussion and interaction in which work plans were established for institutionalization of family businesses in order to strengthen succession processes.

Thanks to the knowledge of business vocations in their states, their performance as promoters of Nafin and business activity of each advisor, Advisory Councils represent the main reference for a “Survey for Identification of National Procurement”, one of the main initiatives of Nafin’s Deputy General Directorate for Regional Promotion and Institutional Relations in 2017, since it is a diagnostic tool for decision-making aimed at strengthening of the domestic market for companies and investors, raising the productivity of its surroundings. This initiative was complemented by joint Advisory Councils between advisors with similar business interests. These meetings were held between Advisory Councils of Durango and Sinaloa, Nuevo León and Tamaulipas, as well as Durango and Nuevo León.

Credit for Young People

This initiative, which was presented in February 2015, aims to promote financial

inclusion and economic growth through access to financing at preferential rates in four different modalities. With the Financial Reform it is possible to support young people without a credit history and wishing to access financing services, with amounts ranging from 50,000 to 2.5 million pesos, for young people between 18 and 35 years of age. In 2017, 2723 loans were placed with an amount of 1.140 billion pesos.

Likewise, in March the planning of the launching strategy “Applicando México” began,

an initiative that promotes digital culture in young people, with which the registration of 144 projects was achieved.

Women’s SMEs (Mujer Pyme)

At 2017 end, 4188 loans were channeled for a total of 4.705 billion pesos. Additionally, “Alianza Contigo” program was launched, an initiative created to generate links among all business organizations, associations and institutions of business women, as well as mapping this ecosystem. ¶



-1,04 %

9439,13

16	2167,57	1,8	10	274,25	1,0	114,69	1,72
23	2563,05	-0,70	11	274,25	1,0	4,14	86,33
14	274,97	-1,6	12	274,25	1,0	16,34	116,22
82	273,05	-0,79	13	274,25	1,0	22,52	4,19
57	1130,40	-0,85	14	1124,65	-0,79	41,43	16,62
7,45	1128,61	-0,75	15	650,82	-0,64	52,31	22,11
7,5	711,08	-0,75	16	354,57	+1,2	38,50	41,37
14,1	346,85	-0,75	17	1413,94	-3,4	108,32	52,60
2	1265,09	-1,0	18	7661,90	-11,5	0,91	37,82
14,1	6676,40	-1,9	19	66004,48	-12,9	16,34	0,90
14,1	63512,93	-0,79	20	457,48	-3,6	38,12	16,13
14,1	435,80	-0,15	21	2721,95	-4,3	16,13	38,00
14,1	2728,12	-1,4	22	5893	+0,23	154,85	1,39
14,1	5981,73	-1,1	23	98	+1,5	1,39	22,46
14,1	9920,40	-2,5	24	98	+0,80	41,68	18,47
14,1	9920,40	-3,5	25	98	-0,84	18,47	18,61
14,1	9920,40	-0,84	26	98	-0,84	18,47	18,44
14,1	9920,40	-0,84	27	98	-0,84	18,47	18,44
14,1	9920,40	-0,84	28	98	-0,84	18,47	18,44
14,1	9920,40	-0,84	29	98	-0,84	18,47	18,44
14,1	9920,40	-0,84	30	98	-0,84	18,47	18,44

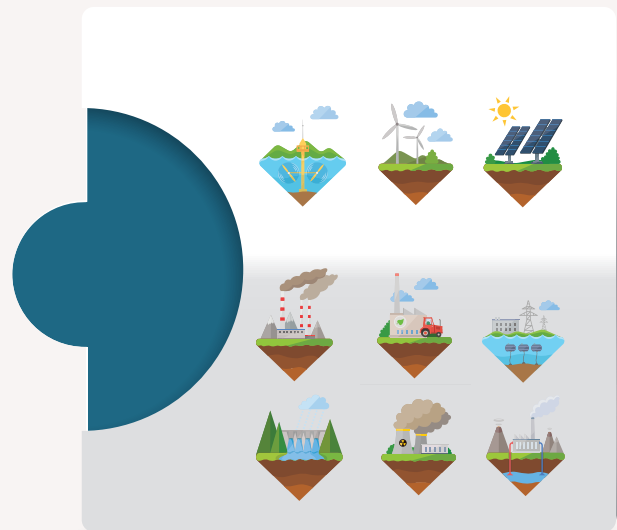
INVESTMENT BANKING

Guarantees on Securities Instruments

- Nafin maintains a Stock Exchange Guarantee Program (PGB) in force, with the aim of continuing to encourage companies to improve their credit rating by issuing a stock market debt and obtaining greater depth in the market, allowing them to place it at longer maturities and amounts by accessing a larger segment of investors.
- During 2017, the issue of a broker was paid for 112 million pesos, guaranteed by Nafin at 40%.
- Nafin continues with the promotion of Stock Exchange Guarantee Programs through stock brokers, the Mexican Association of Stock Exchange Brokers and Mexican Stock Exchange (BMV), among others, in order to boost stock market debt markets in Mexico.

Structured Credits

This is a mechanism through which financing is granted for a specific purpose vehicle, in which companies monetize their asset portfolios, allowing to isolate operating risk



and obtain higher credit ratings, without affecting their balance. This program is aimed at medium and large companies that generate portfolio with collection rights.

Petrochemical Company in Veracruz

It follows up on a simple corporate credit for 240 million dollars, authorized to rehabilitate and start up a fertilizer plant, a priority project for Mexico that will replace imports.

Decentralized Public Organization

Authorized lines to government agencies is followed up, with a balance of 1 billion pesos.

Supply Chain of Federal Electricity Commission (CFE) with support to Mexican suppliers of Electrical Infrastructure in Sonora

During 2015, a financing was granted in favor of a Mexican consortium for the development of a Financed Public Works Contract whose purpose was to design, construct and start up seven transmission lines, with a length of 426 km, and five electrical substations associated with the construction of “Empalme I” Combined Cycle Power Plant, in the state of Sonora. By 2017 end, 100% of loan was paid, having successfully achieved the project’s start-up.

Boost to Stock Market

Through ABS, or Asset Based Structuring, the first storage line was granted for 3.7 billion pesos in favor of a capital market vehicle. This type of product allows companies to have their financial assets mature to subsequently be placed in debt markets. In a syndication led by Nafin, commercial banks complemented financing of up to 5 billion pesos.

Financial Advisory Services

During 2017, three requests for technical assessments were handled for logistics companies, cement industry and Spanish-speaking media, which relied on placing in the stock market Certificates of Ordinary Participation (CPOs).

Government Banking

During 2017, administration of loans granted to two State Productive Enterprises, Petróleos Mexicanos (Pemex) and CFE, was maintained.

Financing of Projects

Petrochemical Company in Coatzacoalcos

During 2017, authorized credits in favor of a petrochemical complex in Coatzacoalcos for the production of high and low-density polyethylene are monitored: 1) Senior line for an amount of 280 million dollars, 2) line in current account for the purpose of financing Value Added Tax (VAT) derived from investments made during the project’s construction period, for an amount of 30 million dollars, and 3) working capital simple credit for 40 million dollars.

This project was awarded with the Best Projects Award, given by the specialized journal *Engineering News-Record* (ENR), as it is one of the projects with the greatest economic and social impact in the world.

Gas Pipeline Project for Pemex in Center-South of Mexico

Nafin follows up on this project structured with Banobras and participating commercial banks, with a cost of approximately 1.1 billion pesos. The project has an extension of 290 km, from San Luis Potosí to Guanajuato. Resource provisions have been made in accordance with the project’s work schedule.

Gas pipeline for Pemex in the North of Mexico

Nafin follows up the North Phase of this System, which will have an extension of about 453 km (including Nuevo León, Tamaulipas and San Luis Potosí). The project will cost approximately 1.518 billion dollars, where Nafin participates with 240 million dollars, and we are just waiting for the declaration of the system’s commercial operation. 100% of the credit line has been disbursed.

Support to a Company in the Telecommunications Sector

In 2015, in order to promote the development of telecommunications infrastructure at national level, a financing was granted to a company that develops the transmission network and promotes Internet coverage in Mexico. During 2017, the financing derived from placement in the debt market was paid off.

Small Hydroelectric Plant in Nayarit

The first hydroelectric plant financed by Nafin is monitored, with an installed capacity of 28.8 MW in the state of Nayarit. The hydroelectric plant belongs to CFE Hydroelectric System on the Santiago River and had a cost of approximately 1 billion pesos.

Wind Farm in Puebla

A wind farm of 66 MW installed capacity in Puebla is monitored. From this project, Nafin began a relationship with a leading private producer of energy in Mexico and in the world.

Hydroelectric Power Plant in Puebla

The second hydroelectric plant financed by Nafin is monitored, with an installed capacity of 36 MW in the state of Puebla. Through this financing, Nafin strengthens its financing network aimed at hydroelectric generation plants.

Third Long Term Auction

In 2017, financing was authorized for up to 292 million dollars for the construction and start-up of an open-cycle power plant, which will provide power under the coverage contract SLP-1/2017. The project is relevant

as it is the first to complement a clean energy supply under an auction scheme.

Sustainable Projects

In line with Federal Government objectives to promote Sustainable Development in Mexico, embodied in the National Development Plan 2013-2018, Nafin promotes financing and investment schemes from various sources aimed at generating electric power projects from renewable energy sources and clean technologies, to optimize the use of public investment as a complement to private investment, in order to contribute actively in new scopes, responsibilities, investment requirements and expected goals of the energy sector, derived from Mexico's Energy Reform. During 2017, the following projects stand out:

Shared Network

In March 2017, a simple credit agreement for 5.5 billion pesos was formalized to finance a wholesale broadband services network project that will market capacity, infrastructure and telecommunications services to concessionaires and marking companies. The Mexican development banks participate with up to 17.75 billion pesos through Banobras, Nafin and National Bank of Foreign Trade (Bancomext). The first provision was made in June.

It is estimated that this Shared Network will allow access to the most advanced 4G-LTE technology to at least 92.2% of the Mexican population; currently it is only half.

This deployment is being finalized through a Public-Private Partnership. According to the plan, it is estimated that in March 2018 it will start offering its services to 30% of the

population; by the end of 2021 it will be extended to 85%; and will be completed in January 2024, when 92.2% of the population will have access to the most modern and efficient broadband network in the Mexican market and internationally.

Wind Farm of 396 MW

In May, a simple loan for 1.35 billion pesos was formalized for the financing of VAT caused by investments required for the construction of a wind farm in the state of Oaxaca, with an installed capacity of 396 MW.

874 MW Combined Cycle Plant

In June, a simple loan of 2 billion pesos was formalized for the financing of VAT caused by investments required for the construction of a combined cycle plant in the state of Jalisco, with an installed capacity of 874 MW.

Wind Farm up to 442.8 MW

In August, two simple loans were formalized to finance (i) the construction and operation of a wind farm in Tamaulipas with an installed capacity of up to 442.8 MW, for an amount of 110 million dollars; and (ii) VAT derived from investments required for the construction of this project in the amount of 1.034 billion pesos. Nafin participates in the project as agent bank of VAT credit.

178.9 MW Photovoltaic Solar Plant

In September, two simple loans were formalized to finance (i) the construction and operation of a photovoltaic solar plant in Chihuahua, with an installed capacity of up to 178.9 MW, for an amount of 27.3 million dollars; and (ii) for VAT derived from investments required for the project's construction, for an amount of

264.5 million pesos. Nafin participates in this project as agent bank.

158.4 MW Photovoltaic Solar Plant

In September, two simple loans were formalized to finance (i) the construction and operation of a photovoltaic solar plant in Sonora with an installed capacity of up to 158.4 MW, for an amount of 24.3 million dollars; and (ii) for VAT derived from investments required for the project's construction, for an amount of 230.5 million pesos. Nafin participates in this project as agent bank.

Wind Farm of 250 MW

In October, a simple loan of 500 million pesos was formalized for financing of VAT caused by investments required for the construction of a wind farm in the state of Nuevo Leon, with an installed capacity of 250 MW.

65.3 MW Photovoltaic Solar Plant

In December, the financing of a photovoltaic solar plant in Chihuahua was formalized with an installed capacity of up to 65.3 MW, having two specific purpose companies as co-credited through the following transactions: (i) simple credit for the construction and operation of this project, for an amount of 593.8 million pesos; and (ii) two simple credits for VAT derived from investments required for the project's construction, for an amount of 55 million pesos each. Nafin participates in this project as agent bank.

Prepayment of Credits

In May, advance payments of two loans granted in pesos were received from a multilateral organization and a foreign financial institution to participate in the financing of a wind farm in Oaxaca, for a total of 439 million pesos.

Results

In 2017, sustainable projects have been added:

- A wholesale broadband services network project.
- A combined cycle plant in Jalisco.
- Three wind farms in Oaxaca, Tamaulipas, and Nuevo Leon.
- Three photovoltaic solar plants in Sonora and Chihuahua.

With this, the presence of Nafin in the energy and telecommunications sectors in Mexico is expanded.

The financing of a Public-Private Partnership project represents the opening of a new business segment of Investment Banking. In addition, Nafin confirms its role as promoter of the Energy Reform, through large-scale financing, aimed at the development of strategic sectors that will help to increase Mexico's transmission infrastructure and electricity coverage.

Investment Programs

Direct Share Investment

Regarding the permanent portfolio of companies, during 2017 different follow-up actions were carried out to Nafin's direct equity investment portfolio. Additionally, seven calls for capital received by a bilateral fund in which Nafin has a stake were handled during the year.

Indirect Stock Investment

Nafin promotes and develops venture capital industry in Mexico, through Corporación Mexicana de Inversiones de Capital, S.A. de C.V. (CMIC or Fund of Funds). CMIC corporate structure is divided into nine vehicles, with specific investments in Private Capital, Venture Capital, Mezzanine Debt and Energy Sector.

As of December 2017, CMIC holds debt for 917.5 million dollars in 82 investment funds and 20 direct joint investments, supporting 198 Mexican companies and more than 67,000 direct jobs.

Also, Nafin participates as a partner of Development Bank of Latin America (CAF), with an amount equivalent to 1.2% of the ordinary capital of that multilateral organization. The chairman of the Board of Directors of Nafin (Ministry of Finance and Public Credit) participates as a member of CAF's Board of Directors, with the aim of promoting financial and technical cooperation schemes for the development of SMEs in our country.

Programs of Institutional Market of Corporate Alternative Debt -MIDAS

In order to be more efficient, Nafin designed Programs of Institutional Market of Corporate Alternative Debt -MIDAS, which combines Nafin's credit support for companies to implement their modernization and expansion plans, as well as stock market promotion through supporting companies so that, in a period no longer than three years, they are candidates to issue debt in BMV through the fulfillment of an institutionalization program of their corporate governance, in order to contribute and strengthen its permanence in the market, as well as providing transparency and certainty to third parties as a future public company.

Accredited companies began with an institutionalization program of their governing bodies to later be able to issue debt in the Stock Market. It is contemplated that during the first semester of 2018 the first issue of a company promoted with the MIDAS program will be placed on BMV. ¶



INTERNATIONAL

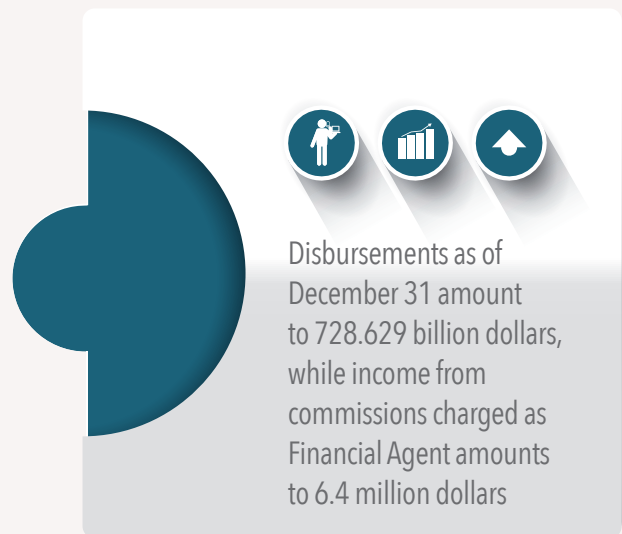
Project Management

At 2017 end, disbursement of resources as a direct borrower of International Financial Organizations (OFI) amounted to 350 million dollars from CAF, 12 million dollars from German Development Bank (KfW) and 100 million dollars from European Investment Bank (EIB) to working capital operations and green financing projects respectively. Financing projects of OFI in force, contracted and in negotiation during the period are the following:

Current Financing of OFI

- **Non-reimbursable Technical Cooperation granted by IDB, ATN/TC-13019-ME amounting 409 thousand dollars for Nafin's institutional strengthening**

In 2017, 75,750 dollars were disbursed, adding an accumulated amount of 364,382 dollars, achieving an 89% advance in the execution of resources. It is planned to make two disbursements of cooperation in the amount of 16,901 dollars and 8,821, thus reaching an accumulated amount of 390,104 dollars representing 95% on the execution of resources. The following steps correspond to the formal cancellation of remaining balances before



Nafin and its authorization, as well as request for closing audit schedules before the Ministry of Public Function (SFP).

Loans and Technical Cooperation of IDB and Clean Technology Fund (CTF) to finance a Geothermal Risk Transfer and Financing Program

The objective is to encourage private investment through financial mechanisms and risk transfer that reduce investment costs, mobilize private capital allocated to projects and guarantee their sustainability/growth in the long term. During 2016 and 2017, the Division of Sustainable Projects, as a business area, carried out identification, promotion

and analysis activities to generate a portfolio of geothermal projects. In November 2017, IDB carried out a special mission, in order to analyze the program's restructuring and take advantage of resources contracted. In this mission participated: Nafin, Ministry of Energy (Sener), SHCP, and CFE.

This mission concluded with a proposal to restructure the program, whose main modifications are the transfer of resources from concessional credit to contingent donation, expansion of disbursement periods and repayment periods. IDB will request these changes from CTF at beginning of 2018, with the purpose of capitalizing on the existing efforts and work carried out to achieve successful geothermal projects under a more competitive cost scheme for current conditions of energy markets in Mexico.

Line from KfW for 31.2 million euros for a Program of Environmental Improvement of SMEs

As of December 31, 2014, 20.4 million euros were disbursed from Tranche I, using all of it. From this amount, 11.7 million euros correspond to Small Transporter Program (Man-Truck), aimed to finance 164 credits granted by a financial intermediary of the Program to beneficiaries that had a scrap certificate. The remaining 8.7 million euros were allocated to the Program for the Environmental Improvement of SMEs in Mexico, granted by the Trust Fund for Saving Electric Energy (FIDE) under the Eco Business Credit Program. Additionally, Tranche II of this line of credit for 10.7 million euros has been disbursed almost in full and the balance at the end of the period is 180,000 euros, which remains in force with

the objective of maintaining the validity of this Financial Contribution complementary to these two tranches.

- **Financial contribution of KfW for 1.02 million euros.** In 2013, an action plan was developed for the institutional strengthening of Nafin and the Eco Business Credit Program, under FIDE's responsibility. At 2017 end, the following actions were taken: consultancies for the Small Transporter Program (Man-Truck), modernization of FIDE Operating Program platform and to support the Division of International Financial Organizations (DOFI) in processes for international contracting; new functionalities to Information System of FIDE's Operational Program; training plan for FIDE representatives involved in the Eco Business Credit Program; hiring indexing services of 20,000 files for FIDE; a market study of MSMEs for this program's positioning; design and implementation of a dissemination plan for the Energy Saving and Energy Efficiency Program; as well as a diploma in energy efficiency and two certification workshops in Project Management for Nafin staff. This has represented an accumulated expense of 800,121 euros. With an available balance of 222,461 euros, it is intended to continue supporting FIDE in its institutional strengthening, highlighting the acquisition of monitoring, reporting and verification equipment; likewise, training activities will be supported for Nafin personnel mainly. In November 2017, KfW authorized the extension to disbursement deadline as of June 30, 2018.

Promotional Financing Line with KfW for 50 million dollars for Renewable Energies

During 2017, contractual commitments to report information, Nafin Consolidated Financial Statements and progress reports of supported project were fulfilled.

- **Financial Cooperation.** As a commitment to contracting this line, KfW committed Nafin to financing the development and implementation of an Environmental and Social Management System (ESMS) tailored to and proportional to its operations, that meets the requirements of national legislation and international standards. With ESMS, Nafin will strengthen its evaluation, mitigation, management, documentation and monitoring capacities of impacts and risks associated with financing and investment and will position itself as a leading institution in green financing. Until the end of 2017, the following actions have been carried out:
 - » KfW carried out a selection process for international consultancy, in which a company called Environmental Resources Management (ERM) was selected.
 - » In November, KfW made a formal presentation of ERM and its proposed work schedule and deliverables.
 - » Consultancy will have a duration of 18 months divided into six months of research and development of the system and 12 months of support (pilot test).

Line not Committed with CAF for 300 million dollars

During 2017, six provisions were made for a total of 350 million dollars, consolidating as one of the main short-term instruments to finance working capital operations.

Financing Contracted in 2017

- **Loan with EIB for 100 million dollars.** As part of the strategy of diversifying sources of long-term funding in dollars, the possibility of contracting financing with EIB was managed. With this purpose, in 2016 EIB performed a due diligence on Nafin, requested SHCP its “No objection” and took to its internal committee the proposal of credit for Nafin for up to 50 million dollars to finance renewable energy projects, obtaining a favorable answer. On March 21, 2017, during the signing of a Memorandum of Understanding (MOU) between Nafin and EIB, executives of both institutions agreed to reach an amount of 100 million dollars. As a result, in the ordinary session of July 2017, a request for an extension of 50 million dollars was submitted to Nafin’s Board of Directors from those originally agreed, which was approved.

On October 31, 2017, the signing of a loan agreement between both institutions was carried out, at European Union (EU) site in Mexico, to support renewable energy projects. Efforts to disburse resources started immediately with the fulfillment of preconditions and in December 2017, all the resources were disbursed. The following actions correspond to the delivery of progress

and compliance reports, with the first interest payment to be made in March 2018 and capital payments in December 2019. For both institutions the signing of this contract was a fact of great importance, as it was the first operation of EIB in Mexico in the last decade.

Along with this loan, EIB will request support from the EU's Latin American Investment Fund (LAIF), with the aim of strengthening Nafin's technical and operating capabilities to encourage and structure sustainable development projects in strategic areas, and programs and services for SMEs, with a social, environmental and economic focus.

- **KfW Concession Financing Line for 56.6 million dollars to Support Water Desalination Projects.** Within a Financial Cooperation between the governments of Germany and Mexico, Nafin agreed to contract an allocation of concession resources, through a credit line from KfW. This allocation is intended to support environmental protection that include water desalination projects. In December 2017, a contract was signed and during 2018 the analysis of water desalination projects will continue, which are intended to be supported with this line during the first semester of 2018. Validity of resources ended in December 2017, so that the signing of this contract allowed the Mexican government to take advantage of concession resources allocation, strengthening diplomatic relationships between Mexico and Germany.

OFI Projects under Negotiation

- **KfW Financing Line for 30 million euros for Forest Investment Program (PROINFOR).**

At SHCP request, Nafin will support Institutional Trusts in Relation to Agriculture (FIRA), to contract a concession loan with KfW, by virtue of not having a sovereign guarantee. This loan will be transferred to FIRA under favorable conditions that KfW is granting, plus operating and risk costs that Nafin generates as broker. In November 2017, an evaluation mission of the Project was carried out, in order to prepare a proposal to the German Ministry of Cooperation and Development (BMZ) for its approval. It is expected to sign this loan line at the beginning of the second semester of 2018. This loan line includes a Financial Contribution for an amount of 6 million euros to support this Program, which will be used in its entirety to develop actions carried out by FIRA.

Concession Financing Lines with KfW for 100 million euros each

Due to the celebration of the Germany-Mexico dual year and with the purpose of supporting actions of our country to mitigate the effects of climate change, the German government allocated concessional resources to Mexico for two topics:

- Support for innovative green financing programs or projects in Mexico. Resources are labeled for actions that Mexico undertakes in this regard and Nafin could consider contracting all or part of said resources through a KfW credit line, to support its potential portfolio of projects to be financed in 2018 and 2019.

- Program for Mitigation of Climate Change in Transportation Sector in Mexico. As part of preparation works to consider contracting this loan, KfW hired a team of consultants to carry out a feasibility study of Nafin programs in such sector. This study was carried out from July 9 to August 19, conducting interviews with internal areas of Nafin and relevant actors of the transport sector (federal, state and municipal governments, chambers, transport organizations, financial brokers, and assemblers). In November, preliminary results of this report were presented to KfW and Nafin, with the conclusion that the most viable proposal with greatest environmental impact is to allocate resources for the replacement of vehicle fleets in the cargo sector, through auctions in which financial brokers wishing to participate must offer the greatest reduction of greenhouse gases. The proposal includes elements that will help position Nafin as a reference in green financing programs, such as compulsory scrapping, the possibility of buying new units and training for hauliers. A final report will be presented in February 2018 and, where appropriate, loan negotiations will begin during the last quarter of 2018. KfW will review the possibility of obtaining financial support resources to support this Program, in case of contracting this line.

Financial Cooperation of Nama Facility Fund/GIZ

The German Agency for International Cooperation (GIZ) is supporting the Mexican government in Country-Appropriate Mitigation Actions (NAMAs), part of commitments to

combat climate change of each country. As for SMEs, they have identified Nafin Business Credit program as a SME NAMA that should be strengthened, so they are making requests for financial cooperation to the Nama Facility Fund to strengthen this program. In 2017, GIZ hired two consultants to carry out a due diligence process to Nafin and prepare such proposal. This proposal was presented in December 2017, with the main intention of supporting with resources to Nafin's guarantee fund and financing of some energy diagnoses for potential projects. The objective is to support Individualized Eco-Credit Programs, prove the feasibility of financing energy efficiency projects, reduce greenhouse gas emissions in Mexican SMEs and strengthen Nafin's capabilities in terms of international resource management and green financing. Nama Facility Fund answer to support the Program is expected during the second quarter of 2018.

International Cooperation

Inter-American Development Bank (IDB)

Nafin participated in the 58th Annual Meeting of IDB-CII Assemblies of Governors, which took place from March 30 to April 2 in Asunción, Paraguay. In addition to participating in Annual Meetings, several bilateral meetings were held with institutions such as Standard Chartered, HSBC, International Finance Corporation (IFC), Latin American Association of Development Financing Institutions (Alide), Crédit Agricole, Bank of America, Nomura, Agence Française de Développement (AFD), Mizuho and Banco de la Nación Argentina, in which the existing business relationship was discussed and new cooperation alternatives were explored.

Latin American Association of Development Financing Institutions (Alide)

The 47th Ordinary Meeting of Alide General Assembly was held from May 30 to June 2 in Santiago, Chile. The central theme was “Technological disruption, financial intermediation and financing for development: challenges in an era of change”. In this event, Nafin General Director was appointed Vice Chairman of Alide Board of Directors for 2016-2018, due to strategic links generated in this administration between Nafin and Alide. As such, Nafin Director General led the 47th General Assembly. Likewise, he participated as a panelist in a presentation on “Technological change and economic transformation in Latin America and the Caribbean: Actions of a development bank”, together with representatives of IDB and Latin American development institutions, as well as Chile and Brazil.

Also, Nafin attended an event called “National Banks of Development and Green Banks: Key institutions to mobilize financing and comply with Determined National Contributions and Sustainable Development Goals”, organized by Alide, Banobras, IDB, Green Bank Network and the Organization for Economic Cooperation and Development (OECD), on June 27, in Mexico City. We also participated in the panel “Opportunities to promote capital markets and mobilize institutional investment”, sharing Nafin experience with issuance of the first Green Bond in Mexico and the first Green Bond in pesos. Bilateral meetings were also held with EIB, Green Climate Fund (GCF) and Green Investment Bank (GIB) of the United Kingdom, to follow up on Nafin’s relationship with each of these institutions.

Nafin, through DOFI, participated in the “Seminar on the Promotion of Financial Inclusion through Innovation Policies of a Development Bank”, which took place on August 16 and 17 in Lima, Peru, organized by Alide and the Economic Commission for Latin America and the Caribbean (ECLAC). This event’s objective was to advance the topic of financial inclusion as a productive development policy and analyze the role that development banks can play in the design of instruments and financial innovation to promote financial inclusion of SMEs.

Likewise, our Treasury Division participated in the “Mission of Development Bankers of Latin America and the Caribbean. Energy Efficiency in Germany and its Potential in Latin America and the Caribbean”, which was held in September and included a visit to several cities in Germany to learn about energy efficiency projects financed by KfW. The objective of this meeting was to increase the knowledge of participants in energy efficiency processes, as well as to generate a space for the exchange of best practices, experiences and knowledge in the field of green financing.

On September 6, 2017, Nafin’s General Director assumed the Presidency of Alide Board of Directors, which will continue until the next election of the Board, which will be held at the 48th Regular Meeting of Alide’s General Assembly, in May 2018 in Lima, Peru, and where its 50th anniversary will also be celebrated. In his capacity as President, Nafin’s General Director participated in the CXLV Meeting of the Board of Directors held on October 13 in Washington, DC, United States, and where the status of Alide’s internal work program was reviewed, among others themes.

Montreal Group

The 6th Annual Meeting of the Montreal Group was held in Helsinki, Finland, on June 7-9, with Finnvera hosting the meeting. DOFI participated in the event, as a representative of Nafin before this Board of Directors, and our Product Development Division, to attend meetings of working groups. In preparation for this event, Nafin worked with other members of the Montreal Group in these sub-working groups agreed for the 2016-2017 period: Green Financing (DOFI), Innovative Products and Digitalization, and Online Services (by our Product Development Division).

For the first time, as part of this Annual Meeting, it was decided to undertake a group to SMEs prior to the meeting, that it was focused on clean tech and the Internet of things. This group, organized by its Secretariat, involved 22 representatives of SMEs from member countries, including Mexico, and 51 Finnish organizations. The two-day program focused on development of business opportunities, networking and on-site visits to leading companies in this sector.

Business Development Bank of Canada (BDC)

Our Market Analysis Subdivision participated in the Round Table of Economists 2017, organized by BDC on September 21 and 22, in Montreal, Canada. The purpose was to carry out an analysis together with participating institutions about main trends and global economic perspectives, effects of global events and their impact on Development Banks, as well as to identify innovation processes that allow promotion of SMEs growth, productivity and investment.

World Bank (WB)

Nafin's General Director and our Deputy General Directorate of Treasury and Financial Markets participated in the Annual Meeting of the Boards of Governors of World Bank-International Monetary Fund held in Washington, DC, United States, on October 9-15. Important financial institutions attend this event with the aim of addressing issues of global interest in finance, economy and social development. In addition to participating in forums organized by WB, several bilateral meetings were held with HSBC, Reuters, Multilateral Investment Guarantee Agency (MIGA) of WB, Fitch, Mizuho, Bank of Tokyo-Mitsubishi, Nomura, Bank of America, Goldman Sachs, Standard Chartered and Daiwa, in which the business relationship was reviewed and new areas of inter-institutional collaboration were explored.

International Institute of Finance (IIF)

The Annual Meeting of IIF was held on October 11-14 in Washington, DC, United States. Nafin participated in this event, which analyzed current issues and innovation for the financial sector, among which include: prospects for global financial services industry, cybersecurity and financial stability, Brexit, politics and economics update, border and emerging markets and the future of finance given technological innovations (Fintech, cryptocurrencies, etc.).

International Development Finance Club (IDFC)

Nafin, through our Deputy General Directorate of Treasury and Financial Markets and DOFI, participated in IDFC 6th Annual Meeting,

which took place on October 15 in Washington, DC, United States. The meeting addressed issues related to green financing, sustainable urban development, access to financing and cooperation for development. At the 6th Annual Meeting, AFD General Director was elected as its new President, who presented a work program for its management. Likewise, the acceptance of Cassa Depositi e Prestiti (CdP) of Italy, International Investment Bank (IIB) and Investment and Foreign Trade Bank (BICE) of Argentina as new Club members was formalized.

Cooperation Agreements

European Investment Bank (EIB)

On March 21, 2017, Nafin's General Director and EIB Vice President signed an MOU with the objective of exchanging knowledge, experiences and best practices in green financing and support for SMEs. This MOU was signed within negotiations for a line of credit for Nafin, aimed at supporting renewable energy projects, to strengthen the relationship between both banks and explore collaborative alternatives that contribute to institutional strengthening.

Compañía Española de Financiación del Desarrollo (Cofides)

On July 12, 2017, Nafin's General Director and Cofides President signed an Intention Agreement that aims to cooperate in the identification and support of development projects of MSMEs that maintain business relationships between Spain and Mexico, through presenting all products that both banks have. In addition, Nafin and Cofides agreed to the creation of a new financial product that seeks to promote

the development of investment projects in Mexico. Through this product, Cofides would provide financial support to MSMEs through capital or quasi-capital instruments to carry out commercial or productive implementation in Mexico, while Nafin could participate with guarantees to facilitate the financing of local entities. With regard to large investment projects, Nafin could participate through first-tier financing, while Cofides would support through equity holdings.

Instituto de Crédito Oficial (ICO)

In September 2017, Nafin General Director visited Madrid, Spain, during which an MOU was signed with ICO, with the aim of strengthening cooperation between both banks. Our Director General participated in the "Financial Meeting on Opportunities in Mexico", attended by Spanish businessmen interested in investing in Mexico, to know economic prospects and the role played by Nafin in the support to priority projects. Likewise, a meeting was held with representatives of the Spanish Association of Capital, Growth and Investment (Ascri) and the Fund of ICO Funds (AXIS), to share experiences on the subject and explore potential areas of collaboration between both institutions.

Latin American Association of Development Financing Institutions (Alide)

Given the appointment of Nafin's General Director as President of the Board of Directors, and our active participation during this year in Alide events, both institutions decided to sign a Cooperation Framework Agreement whose objective is to strengthen the collaboration between Nafin and Alide, encouraging the strategic coordination of activities in support

of financing economic and social sectors in Mexico.

Exchange of Best Practices

German Development Bank (KfW)

During the Dual Year Mexico-Germany 2016-2017, Nafin, KfW and GIZ co-organized the conference “Climate and environmental financing: opportunities and challenges for German and Mexican development banks”, which took place on April 25 and 26 at Nafin facilities in Mexico City.

This conference’s purpose was to generate a forum for dialogue between domestic and international experts on the role that development banks can play in financing against climate change and promoting sustainable development, while raising awareness among participants about opportunities, challenges and risks that can be faced when positioning development banking as a strategic actor in the promotion of green investments.

The first day opened with the workshop “How is a green development bank?”, which was attended by 42 experts from development banks, while on the second day the seminar “Development banking: provider of financing services to combat climate change and promote sustainable development”, which brought together 221 expert participants from development and commercial banks, academics, government and private sector representatives from Mexico and Germany, as well as international experts.

International Program on Best Practices for Development Banking: The Nafin Model

For the third consecutive year, the Deputy General Directorate of Treasury and Financial

Markets, together with our Deputy General Directorate of Finance and Management and the Technical Coordination of the CEO, organized the “3rd International Program on Best Practices for Development Banking: The Nafin Model”. The objective was to share Nafin’s experience and best practices in policies, methodologies, programs and products, in addition to presenting our strategy to foreign development banks. This year we had 33 participants from 17 institutions, mainly from Latin America, as well as Spain, Japan and Saudi Arabia.

London School of Economics and Political Science (LSE)

As of 2015, our Deputy General Directorate of Treasury and Financial Markets and LSE have worked on a three-year program, which considers the participation of a Nafin official in postgraduate courses, as well as the preparation and publication of a research article useful for Nafin. During this second year, the designated official focused on green financing, particularly focusing on the carbon market. Such publication will be carried out during the first semester of 2018 and will give continuity to works previously prepared with LSE.

Green Climate Fund (GCF)

Nafin has continued with the accreditation work as Domestic Implementing Entity of GCF. During 2017, a translation was made of documents that will serve as support to demonstrate that requirements established by GCF in fiduciary matters, project management, environmental safeguards and gender are met. Likewise, information was uploaded to Online Accreditation System (OAS) and the

application was sent to GCF Secretariat in July of this year. After a first review by GCF, in December, the fund sent an accreditation fee that Nafin must cover to continue with the process and thus enter a first stage of review of this application.

Financial Agent

As of December 31, 2017, the portfolio as Financial Agent in execution is made up of 20 loans: seven from International Bank for Reconstruction and Development (IBRD, the original World Bank institution), 10 from IDB and three from International Fund for Agricultural Development (IFAD). As well as for seven donations: five from IBRD and two from IFAD, for a total amount of 5023 million dollars.

During the first quarter of 2017, a loan was formalized with IDB for an amount of 600 million dollars for the Program to Support the Strengthening of PROSPERA, to be executed by its National Coordination.

Six loans were negotiated:

- Program for Construction and Equipment of the National Animal Health Reference Center for 145 million dollars, with IDB.
- Program to Strengthen Treasury Management in Federal Entities and Municipalities for 612.4 million dollars, with IDB.
- Program to Strengthen Treasury Management in Federal Entities and Municipalities for 37.6 million dollars, with Chinese Fund.
- Project to Strengthen Access to Social Housing for 100 million dollars, with the World Bank.

- Project for a National Agri-food Storage System for 130 million dollars, with the World Bank.
- Higher Education Project for 120 million dollars, with the World Bank.

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

- Four loans with IDB to support an Employment Support Program, for a tentative amount of 200 million dollars, to be executed by Ministry of Labor and Social Security (STPS); Community Education Program for Basic Education Schools, for a tentative amount of 80 million dollars, to be executed by National Council for Educational Promotion (Conafe); Energy Efficiency Measures Program in Real Estate of the Federal Public Administration, amount to be defined, by Sener; and Strengthening Program for Urban Infrastructure, for a tentative amount of 500 million dollars, under the responsibility of Ministry of Territorial and Urban Development (Sedatu).
- A loan with the World Bank to support an Energy Efficiency Project in the Agricultural Sector, amount to be defined, to be executed by Sener in conjunction with the Shared Risk Trust (Firco).
- A loan with IFAD to support a Social Economy Project, Development of Inclusion Territories, for a tentative amount of 35 million dollars, in charge of National Institute of Social Economy (INAES).

It is important to clarify that SHCP will confirm the amounts of loans once indebtedness ceilings

have been confirmed and budgets assigned by agencies when negotiating such operations.

Derived from this, 45 missions of preparation and supervision of OFI have been attended, of which 15 were field visits, on the one hand. On the other, 14 procurement training workshops have been given on external credit to executing agencies, as agreed between OFI and SFP.

It is worth mentioning a visit made by World Bank officials to review Forest Investment Program (FIP) results, which is supported with resources of Grant TF-010261, in which field observations were made on advances in FIP and execution of financed activities, determining that they were met satisfactorily on schedule. Nafin, as Financial Agent, has worked jointly with the Mexican Forestry Commission providing technical assistance and training in procurement matters, with the purpose of having hiring processes carried out in accordance with regulations applicable to

procurement using foreign credits and eligible for resources from said Grant.

Finally, a Work Meeting on Acquisitions and Financial Management organized by the World Bank was held, with the participation of IDB, SFP, executing agencies and financial agents, in which the agreements assumed in 2016 on the new Regulatory Framework for Bank Acquisitions were reviewed, as well as determining dates to start negotiating said regulations with the Mexican government. In this sense, SFP highlighted Nafin participation, as representative of SHCP as Financial Agent, in the negotiation and implementation of agreed documents on foreign credits.

The main sectors financed by financial organizations are: energy, agriculture, social, education, environment, climate change and health. Disbursements as of December 31 amount to 728.619 billion dollars, while income from commissions charged as Financial Agent amounts to 6.4 million dollars. ¶



TREASURY AND MARKETS

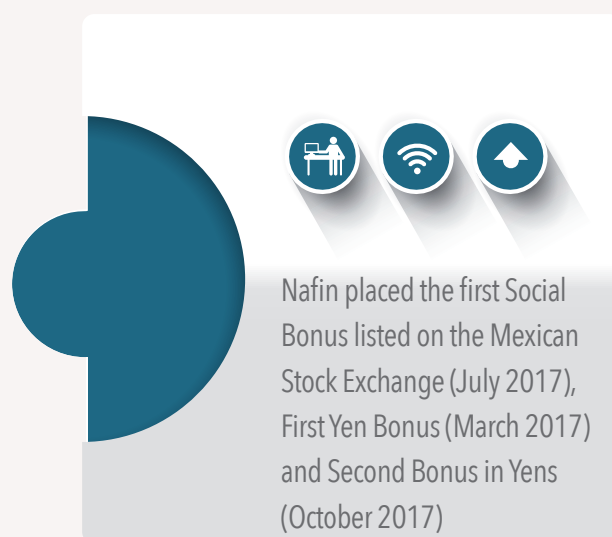
Treasury

Funding

To ensure that Nafin always has sufficient resources and can disperse them to different business areas in the best conditions of cost and terms, Treasury carries out a strategy based on the diversification of funding sources and on derivative hedging operations.

Continuing with the strategy that began in 2013, during 2017 Treasury issued Stock Certificates for Development Banking through a syndicated auction mechanism, which has allowed to:

- Improve liquidity conditions.
- Develop a debt curve as Development Bank to longer terms, transmitting funding benefits to the industry.
- Promote an integral development of securities market and the Mexican financial system.
- Promote efficiency of local public debt markets, seeking at all times to make efficient the price discovery process.
- Have a greater participation of investors.
- Improve operating dynamics in secondary markets.
- As of December 31, 2017, 57 billion pesos of Nacional Financiera Certificates are outstanding, of which 47 billion pesos were issued through syndicated auction,



11.55 billion pesos at three years and variable interest rate, and 35.45 billion pesos at a 10-year term and fixed interest rate.

Regarding foreign currency, our Certificates of Deposit Program at Nafin's London Branch continued to be mainly used which, together with the acquisition of interbank financing lines, time deposits and working capital lines, in addition to a pair of Japanese yen issues in the Asian market, allowed Treasury to maintain its funding cost at attractive levels, according to our goals.

Cebures-Euroclear

Continuing with syndicated auctions, in

April Nafin carried out the issuance of a new series of Stock Certificates for Development Banking at a three-year term variable rate, as well as reopening of long-term fixed-rate ones, which can be settled through Euroclear and Clearstream. It should be remembered that this scheme provides international investment public access to these debt certificates. The amount placed in this syndicated auction in April was 6 billion pesos in communicating vessels, with 1.25 billion pesos allocated in the fixed tranche, so that this issue settled through Euroclear and Clearstream currently has a total amount of 10.45 billion pesos.

These actions take place according to the 2017 Operating and Financial Program, which contributes to Mexico's economic development by facilitating access to financing for MSMEs, as well as fostering financial markets.

Social Bonus

In July 2017, in accordance with its strategy of developing the stock market and supporting Mexico's social sector, Nafin placed the first Social Bonus listed on the Mexican Stock Exchange, which has a second opinion. This transaction had a total demand of 13.373 billion pesos, which represents an oversupply of 3.34 times compared to the total amount placed, i.e. 4 billion pesos, and 6.68 times our target amount, i.e. 2 billion pesos. The placement rate had a differential with respect to Mexico's 28-day Interbank Interest Rate of Equilibrium (TIE), of minus 2 bp for a term of five years. This instrument obtained a rating of AAA (or its equivalent) on a local scale by five rating agencies: S&P, Moody's, Fitch, DBRS and HR.

For this issue, resources will be used to finance programs with social goals, among which are education issues, financial services for low-income and marginalized populations, loans granted to women entrepreneurs or financing for MSMEs, improvement of existing housing, support for MSMEs economic recovery or companies affected by natural disasters.

Nafin Social Bonus is aligned with the 2017 Principles of Social Bonds (Social Bond Principles) of International Capital Market Association (ICMA), due to the nature of eligibility criteria for programs and populations supported. Additionally, it contributes to UN's Sustainable Development Goals (SDG), in the fight against poverty; inclusive education; gender equality; decent work; as well as sustained, inclusive and sustainable economic growth. This Social Bonus has the Second Opinion of Sustainalytics BV, a provider of research and analysis of environmental and social governance, which evaluated this instrument to ensure that it is aligned with Social Bonus Principles.

With this Social Bonus, Nafin continues as a pioneer in the field of thematic bonds, remembering that in 2015 we returned to international markets with the issuance of a green bond in dollars and in September 2016 issued a green bond in pesos.

First Yen Bonus

During March 2017, Nafin reappeared in the international debt markets, this time making a first issue, since the 90s, in the Japanese market of a bond in yens, for an amount of 10 billion, at a five-year term with a coupon rate of 0.78%, which was equivalent to a dollar rate of L3m+157 bp.

Second Bonus in Yens

As a result of a great acceptance by Japanese investors, a second bond was issued in yens. Placement amount was 15 billion yens, equivalent to 131 million dollars approximately, with a term of five years with three months and a coupon rate of 0.66%, 12 bp below the first bond, which was equivalent to a rate in L3m dollars+130 bp. With this bond, Nafin presence in Asian markets is consolidated.

Balance Management

Our strategy of minimizing Nafin balance sheet exposure to movements in interest rates was maintained, making necessary hedges to protect income received as a financial margin, thus fulfilling Treasury objective to ensure that Balance risks are within approved limits, thus strengthening Nafin's capital.

Investments

In Mexican currency, a maturity portfolio is structured mainly with Federal Government securities, which supports income generation; a liquidity portfolio, composed mainly of government securities and used as collateral in Banxico's payment systems, as well as a portfolio of corporate securities that contributes to the development of private debt markets.

The generation of profits by way of financial margin in dollars has come from portfolios of investment at maturity and available for sale; strategic assets that have remained as one of Nafin balance coverage instruments by hosting long-term deposits. Both portfolios are maintained, practically in their entirety, in United Mexican States Bonds (UMS), as well as state-owned companies, such

as Pemex and CFE. During 2017, investment portfolios in foreign currency achieved revenues of around 151 million pesos.

As regards liquidity portfolio in foreign currency, taking advantage of conditions in international markets, our main strategy has been to optimize profitability of surpluses in US dollars, through the execution of synthetic investments in pesos. However, management of liquid resources through our checkbooks, and particularly through sight and time deposits with development and commercial banks, has allowed us to generate around 49 million pesos of profit.

London Branch

In January 2017 we concluded the registration of Certificates of Deposit (CDs) in the National Banking and Securities Commission (CNBV), with which this instrument can be reported and offered in the local Mexican market. This improvement is in line with the diversification strategy of client portfolio and was reflected by increasing the base of counterparties that have current balance in the Program. Likewise, the number of institutions authorized to operate with our London Branch was increased.

This Branch's efforts in relation to increase balances, as well as in the promotion and search of new clients, have shown positive results, to such a degree that today one of every three dollars received by Nafin comes from this CD Program. During 2017, a modification of this program's amount from 2 to 3 billion dollars was formalized, as well as its extension to a maximum term of 10 years. The maximum historical balance of the Program was recorded at year end, with an amount of 2.073 billion dollars.

With respect to placement and issuance of CDs with maturities greater than one year, it is worth noting that in March and August, two issues were placed in dollars with a foreign counterparty for a term of five years, which allows improving the maturity of liabilities, thus reducing existing gaps in Nafin's balance sheet with attractive borrowing costs that distinguish CD Programs.

In order to comply with British regulatory provisions and in line with best practices, our London Branch has continued with the development of a review and monitoring system during 2017. With this purpose, our Branch acquired an independent consulting service to comply with these obligations, where it constantly works to comply with applicable regulations.

Markets

Promotion

During the second semester of 2017, market promotion activities were directed to new strategies to increase income and profitability of portfolios of our Deputy General Directorate of Treasury and Financial Markets. The strength of client portfolio, together with active promotion works, made it possible to cover in outstanding manner new activities, goals assigned to this area and ensure new resources at competitive levels for Nafin's promotion programs.

During 2017, the following was achieved:

- Exceed our budgeted revenue goal, through operations carried out with Money and Exchange desks, Treasury and market promotion customers.

- Reactivation of inactive clients, determining target products in which it is desired to increase business relationships.
- Expand base of investors, achieving formalization of contracts with new clients.
- Integration of all divisions of our Deputy General Directorate of Treasury and Financial Markets in Nafin Web page, with information of all the corresponding financial products and services.
- A greater demand for trading operations was achieved among promotional customers, with the support of Money Desk, Treasury and brokers.

Through promotion works with customers, placement of our First Social Bonus was supported through a Public Offering in July, contributing our customers with 56% of the total amount allocated.

Financial Markets

During the first quarter of 2017, volatility in financial markets remained at relatively low levels and continued to decline to historical levels throughout the year. Although there were some outbreaks, it can be said that, as measured by VIX index of options on S&P 500, 2017 was the least volatile year in the history of this indicator.

The price of oil that rose slightly in the first quarter, then fell in the second quarter, had a bull run in the second part of the year. The West Texas Intermediate (WTI) ended above 60 dollars per barrel, the highest closing price since 2013, which meant a recovery of 12.5% for the year.

US equity markets performed very favorably, encouraged by expectations generated by Donald Trump's expansionary fiscal proposals, particularly the one regarding corporate tax cuts. Dow Jones index advanced 25.1%; S&P 50, 19.42%, and Nasdaq, 28.2%. Other markets also made significant progress in expectations of economic growth without inflationary pressures; FTSE 100 index of the London Stock Exchange grew 7.63%, Dax of the German stock market rose 12.5% and Bovespa of Sao Paulo stock market rose 26.9%.

In terms of interest rates, a 75 bp increase in reference rates by the Fed was transferred to yield curves. While Treasury bonds rates of periods between two and five years registered increases of 69, 51 and 28 bp, respectively, those of 10 years fell by 4 bp and those of 30 years did by 33 bp. These last two terms, however, had increases of 46 bp and 22 bp, respectively, due to discussions on the tax reform and its subsequent approval in December, expecting greater deficit and indebtedness that will generate tax measures that would be adopted from the beginning of 2018.

In terms of currencies, 2017 was not a good year for the US dollar, having a differentiated behavior with other currencies. In general terms it depreciated 9.9%, after three consecutive years in which it accumulated an advance of 27.7%.

At local level, uncertainty was giving ground to the extent that President Trump modified his aggressive speech about NAFTA and negotiations began to modernize this Agreement. Chances that the United States would abandon NAFTA had a negative impact on growth expectations for the Mexican economy in 2017 and led to an accelerated

depreciation of our exchange rate after US elections.

The risks seemed to be transferred more domestically, mainly due to a rise in inflation and consequent increases in Banxico's target rate.

Long-term rates, not without fluctuations, showed a steep downward trend, despite a 125 bp increase in the monetary policy rate. The anchoring of medium-term inflation expectations contributed to this behavior. At year end, an inverse formation was observed in the yield curve.

Exchange rate, after reaching its historical maximum level in January, exceeding 22 pesos, showed an accelerated and continuous decline.

In the stock market, the Mexican Price and Quotation Index (CPI) began with a moderate rise to later have more dynamism and break the barrier of 50,000 points in intraday operations in April and May. The improvement in growth expectation supported this behavior.

Money Market and Bonds

The beginning of 2017 showed a rather negative outlook for Mexico and fixed income markets, due to the following factors: a) increase in gasoline price had rapid effects on consumer confidence, social protests and Monetary policy decisions of Banxico; b) uncertainty about risks of a rapid slowdown in the economy also impacted the mood of investors and, c) Donald Trump victory in elections of the United States.

Banxico pushed its target rate with five increases during the year, which went from 5.75% in 2016 to 7.25% at the end of 2017 (150 bp increase), in trying to stop exchange

depreciation but, above all, inflationary effects caused mainly by an increase in gasoline at the beginning of the year.

In debt markets, portfolios with investment in instruments with terms greater than one year had positive results for a large part of 2017, until October that began to observe the departure of investors. Dec 2024 Bond (seven-year term) registered an increase of 99 bp from its lowest point observed in June (6.61%) to the year-end level (7.60%), which means a decrease in its price. This behavior was similar in most of M Bonds curve. All this due to uncertainty caused by NAFTA negotiations with the United States and Canada, by elections in Mexico in 2018 and by the approved fiscal plan in the US.

Exchange Rate Market

Exchange rate presented periods of high volatility. In principle related to political issues, since uncertainty and speculation caused by presidential succession in the United States generated weakness in the dollar-peso parity, which reached levels above 22 pesos in intraday sessions earlier in the year.

However, monetary policy decisions of Banxico with the objective of controlling inflation, increasing its funding objective rate from 5.75% to 7.25% at year-end six times, made assets in pesos more attractive. In addition, implementation of a program of Non-Delivery Exchange Coverage (NDF) increased liquidity, which caused an adjustment in the price that reached levels below 17.50 pesos in the summer.

The maximum level reached during the year was 22.04 pesos. The minimum was 17.45 pesos and the closing price was 19.6629 pesos.

In the rest of the year, there was still significant activity, although with an exchange rate that fluctuated in lower ranges than in the first half, with peso performance closely linked to news related to NAFTA negotiations.

Forward in the United States, it is expected that modifications of tax policy will stimulate economic activity. Short-term impact in the US will be a consequence, more than anything, of investment responses to cuts in tax rates applied to companies.

For Mexico, periods of additional volatility related to elections news are not ruled out, due to expectations of monetary policy stringency caused by high inflation and agreements reached regarding NAFTA.

Capital Markets

At the beginning of 2017, a great uncertainty prevailed in the Mexican stock market. Cancellation risks of NAFTA by the United States were latent and it was a major factor of concern for investors. However, over the weeks this idea was reconsidered by many market participants, considering that our commercial relationship with the United States is so strong that it could hardly be nullified or even drastic modifications that could substantially affect the Mexican economy are unlikely.

In the first semester, Mexican companies released very positive financial figures thanks in large part to the fact that peso devaluation managed to boost their sales, since almost half of companies' revenues listed on the BMV come from overseas. From April to the end of June, volatility decreased significantly, with the result that the Mexican stock index moved in a narrow range between 49,000 and 50,000 units. In July, CPI managed to

reach a record high of 51,770 points as a result of a general rebound of stock markets, which allowed continuous observation of historical maximum levels in most of leading international indexes.

However, during the last quarter of the year, Mexican shares decoupled from good performance of foreign markets and experienced a considerable drop that led IPC to lose more than 4000 points to reach a significant level of resistance, located at 47,000 units. One factor that contributed to a drastic fall in the market was bad reports in the third quarter by Mexican issuers, which experienced a significant drop in their revenues and a contraction in their margins not seen for several quarters. Towards the end of the year, CPI had a slight recovery with which it managed to end the year in 49,354 units registering a yield of 8.2% during 2017. Our Capital Desk achieved in 2017 profits for an amount of 55.1 million pesos net of funding costs and commissions to brokerage firms.

2018 will be a year full of challenges, given that in Mexico we will have very relevant events that could influence the valuation level of our stock market, such as presidential elections, NAFTA negotiations and the real impact of US tax reform in our economy.

Derivatives Market

During 2017, our Derivatives Desk significantly supported Nafin objectives through development of financial markets, where it has consolidated as a market trader in MexDer derivatives exchange for future contracts of government bonds and IPC; as well as in risk management, since our Desk executed 106 hedging opera-

tions that allow protecting income that Nafin receives as a financial margin.

Investment Funds

Nafin Fund Operator continues to work towards meeting its objective; that is, promote access to securities market of small and medium investors, by distributing shares of 12 investment funds managed, reaching 32 contracts signed with 25 commercial brands in the stock market. At the end of December 2017, it has average assets managed in mutual funds for 20.587 billion pesos.

It should be noted that during this period, our Operator has interacted with Nafin's Deputy General Directorate of Regional Promotion and Institutional Relations of Nafin, through its regional offices, to promote purchase and sale of shares from investment funds it administers, in particular with entities of the Public Administration, such as: state finance departments, public universities and/or Integral Port Administrations (APIs). In addition, it participates in the project called: open architecture, which is a product of our recent Financial Reform and consists of the purchase and sale of shares from investment funds in electronic platforms, so that shares are easily acquired by investing public; all in accordance with the mission of Operator.

Cetes directo (Direct purchase of CETES)

During 2017, a new advertising strategy was implemented for contracting Cetesdirecto, through a new campaign of diffusion through various electronic communication media

including social networks, television, radio and with the support of a sales force. Likewise, the use of APPs was promoted for contracting Cetesdirecto, which allows the public to access easily and safely. Similarly, a permanent presence has been maintained in the Interactive Museum of Economics and KidZania entertainment center, as well as in various exhibitions in Mexico.

All these actions allowed 2017 to be a year with an outstanding performance of

this product, reaching more than 320,000 registered customers, of which more than 183,000 already activated their contract with an investment balance exceeding 6.7 billion pesos, surpassing goals established for the year by more than 65%. Likewise, the total amount of debt placed by the Federal Government in 2017 through Cetesdirecto reached 1.23%, which compared to the previous year's participation of 0.73%, represented an increase of 68.49%. ¶

LEGAL AND FIDUCIARY OPERATIONS

Corporate and Business

Its objective has been to provide certainty in legal processes of credit, in financial markets, venture capital, international affairs and advisory matters. Likewise, support was given to Nafin different areas in the preparation and review of contracts for domestic and foreign operations.

The legal area had important results, including updates to Cetesdirecto distribution channel, advisory activities and review of legal instruments with authorities, other entities of the financial sector, customers and service providers; queries to financial authorities in compliance with applicable provisions, and updating and attention of the Stock Exchange Support Program.

Legal advice to Nafin Fund Operator, an Investment Fund Operating Company, and investment funds it manages, holding of ordinary and extraordinary meetings, meetings of Board of Directors and formalization of contracts.

Legal advice and preparation of legal opinions for participation of Nafin as an investor of debt instruments, such as CEBURES and CKDs, among others.

The review, negotiation, validation and updating of framework contracts for securities purchase transactions was also carried out;



reporto operations; contracts for securities lending, custody of securities and bank deposit of securities in administration and under agent's fees agreements. Additionally, framework contracts for Derivative Financial Operations, ISDAS (International Swaps Dealers Association Master Agreement), entered into with different local and foreign financial institutions, and legal advice was provided in audits carried out by different authorities.

Legal advice, support in updating the Secondary Market Auctions Program (Subasec) was provided to promote liquidity of corporate and government debt securities, including contracting activities with participating brokers and contracting with brokerage companies' suppliers of negotiation systems.

Legal advice was given for (i) reopening of stock certificates, under syndicated auction programs, able to be settled in international markets through Euroclear and Clearstream for fixed rate tranches and under a format known as Regulation S, under the US Securities Act of 1933; (ii) private issuance of bonds in pesos in March and October of 2017, and under a format known as Regulation S, under the US Securities Act of 1933; (iii) issuance of the first Social Bond in Mexico in pesos, which was carried out in July 2017 and whose resources will be used to finance programs with social goals in our country.

Legal attention was given to business and advisory schemes in corporate banking, operations as Federal Government's Financial Agent and international financing that Nafin grants or expects to receive, as well as conclusion of contracts of deposit and collateral to formalize guarantees, in lines of credit and discount lines granted by Nafin through competent instances.

Legal advice has been given to hold necessary documents for Nafin's participation in various corporate financings and infrastructure projects in energy and petrochemical fields.

Derived from Nafin new businesses, it has been necessary to create legal instruments for corporate business schemes, which has allowed Nafin's participation in syndicated loans. Financing has been granted to wind, hydroelectric and other alternative energy projects.

Legal support was provided for a loan granted under Programs of Institutional

Market of Corporate Alternative Debt -MIDAS, as well as legal advice on structured financing with assets support.

Likewise, collaboration agreements have been signed with various public and private institutions.

Legal advice has been provided for credit agreements in which Nafin is recognized by international financing agencies.

Legal advice is given to Entrepreneur Capital Trust, highlighting funds that are winners of Inadem calls.

Government Regulations

Procurement

Nafin fully complied with government regulations that apply to it as a National Credit Company, taking care of legal instruments to achieve a proper development of business in all areas, serving a total of 469 cases, mainly:

- » 205 legal instruments were developed.
- » 144 reviews of bond policies.
- » 20 reviews of calls for award processes.
- » Attention to 12 sessions of Nafin Acquisitions, Leases and Services Committees.

Link to Superior Audit of the Federation (ASF)

In relation to functions that this legal area has as a link with ASF, it is reported that eight audits performed were timely supported, in which all information requirements were answered and meetings attended on presentation of preliminary and final results of said audits corresponding to 2016.

Federal Law on Transparency and Access to Public Government Information (LFTAIPG), Federal Law on Transparency and Access to Public Information (LFTAIP) and General Law on Transparency and Access to Public Information (LGTaip)

During 2017, we worked in coordination with Nafin administrative units (UA) in order to keep all information published in the Transparency Obligations website updated according to applicable regulations. Regarding actions for information loading in the Transparency Portal System (Sipot), Transparency Unit (UT) worked in coordination with Nafin administrative areas so that they could update and/or publish their information in accordance with “General Technical Guidelines for publication, standardization of Information related to Obligations established in Title Five in section IV of article 31 of the General Law of Transparency and Access to Public Information” (General Technical Guidelines). Likewise, information load in Sipot was made in accordance with General Technical Guidelines, depending on the format and conservation period for 2015, 2016 and until the third quarter of 2017.

Therefore, once the first phase of the 2017 Annual Verification Program (PAV 2017) was completed, Mexican Institute of Transparency, Access to Information and Protection of Personal Data (INAI) granted recognition to Nafin for having obtained an average 91.67% in compliance with such obligations. Also, observations and/or recommendations of PAV 2017 were notified to Nafin administrative areas for their knowledge and attention, being concluded in the fourth quarter of 2017.

Transparency Unit held working meetings with administrative areas in charge of updating information in the Mexican Transparency Platform. In those meetings, improvements and new methods to upload information in Sipot were presented, advice was given and doubts were solved with practical examples in the Platform.

Regarding Requests for Access to Public Information and Requests for Personal Data, as of December 2017, 331 requests were concluded and 17 are in process, due to the fact that expiration date in INFOMEX system is in January 2018. Individuals filed 20 review appeals before INAI, which are concluded in accordance with resolutions issued by INAI's Plenary in the following sense: eight confirmed, five amended, four revoked and, finally, three dismissed.

During 2017, UT conducted a review of records registered in the System of Index of Reserved Records (IER) finding that, as of June 2017, Nafin had 3591 records registered and classified, identifying that, in several cases, reservation periods had expired, so it was necessary to make a massive declassification thereof. In June 2017, INAI was requested to update file inventory in IER System. Once received, UT asked five involved areas to review their files and confirm those files that must be declassified.

Likewise, on July 3, 2017, administrative areas were requested to update IER in the first semester of 2017. In this regard, our Technical Committee (TC), in its session of July 24, approved IER in the first semester of 2017 and instructed its publication on Nafin website, in an open format.

INAI requested massive declassification of 2805 files contained in 2859 lines, as well as being eliminated from SIER public view. As of December 31, 2017, Nafin has three records registered in Index of Files Classified as Reserved (IECR) and the next update will be carried out according to the Twelfth and Thirteenth “General guidelines on classification and declassification of information, as well as for preparing public versions”.

Legal and Collecting Disputes and Credit Department

This year, the commitment to promote and direct legal actions to help achieve Nafin objectives as a Development Bank was ratified, in accordance with its applicable legal framework, through provision of legal services, portfolio recovery litigation and design of judicial defense strategies to avoid or minimize economic impacts.

In banking formalization services, we have actively worked with business areas to continue promoting the generation of new business schemes and legal instruments that adjust to market needs to enhance the development of SMEs, as well as support for Financial Intermediaries. In addition to the development of new schemes, during 2017, 486 requests for formalization of banking operations, opinions of politically exposed persons and legal opinions of companies and summaries of faculties were received and attended to.

Fiduciary Operations

As of December 31, 2017, our Fiduciary Division manages 452 businesses, with a trust worth

1.3 trillion pesos, a figure that represents 15% more than at 2016 end and which maintains Nafin as the second trust institution in the country in terms of participation in the fiduciary market, concentrating more than 14% of the total trust estate national-wide and almost 70% of total assets managed by Development Banks.

Of all assets under management, 609.595 billion pesos, equivalent to 45%, corresponds to liquid resources, 112% higher than in December 2016. From this amount, 188.246 billion pesos (31%) is invested in our Money Desk and 7.748 billion pesos (1%) in Nafin Funds Operator, which means a 49% increase in liquid investment of fiduciary businesses in Nafin, compared to December 2016. From the remaining resources, 267.951 billion pesos (44%) is deposited in Federal Treasury and 145.807 billion pesos (24%) is invested with various financial intermediaries.

During 2017, three fiduciary businesses were formed, highlighting Fuerza México Trust, created as an instrument of coordination between private investors and the Federal Government, to join forces and raise funds to support areas affected by September 2017 earthquakes.

Income generated by this fiduciary activity amounted to 192 million pesos, which represents 7% more than our year budget.

In this year, documentation of specifications for fiduciary processes subject to automation was finalized, on which development of a comprehensive fiduciary management system should be supported as from 2018 fiscal year.

In the last quarter, Nafin as Trustee obtained from HR Ratings Agency a HR SF1

rating with a Stable Perspective for the issuing trusts segment, which exhibits the highest capacity to offer fiduciary services within the

HR Ratings scale and is based on an optimal control of legal and operational risk in fiduciary processes. ¶



SUPPORT TO OPERATIONS

Quality Management and Organizational Culture

In order to maintain its dynamic growth and qualitative change, Nafin maintains its strategy of continuous improvement in its Quality Management System (QMS), in the development of human capital, strengthening of risk management and incorporation into its technological platform of adequate systems for the efficient operation of programs.

Quality Management System (QMS)

The first version of the Institutional Quality Standards Manual was published in November 2001, which formalizes our Quality Management System. QMS supports Nafin purpose and strategic direction, by addressing needs with a culture of risk prevention and taking advantage of opportunities, aligning Nafin objectives as quality objectives, which results in a positive effect in meeting external and internal challenges. This dynamism is observed in the following table:



Year	Process	ISO Standard
2012	84	2008
2013	81	2008
2014	81	2008
2015	85	2008
2016	91	2008
2017	93	2015

In November 2017, Nafin migrates and certifies to ISO 9001:2015 all 93 existing processes. New documentation standard facilitated and clarified this transition, incorporating in a natural way corrections and new elements of such Standard.

Quality Operating Committees (QOCs)

One of the most important elements of QMS administration is the participation of our staff in quality self-management of their processes. QOCs meet at least once a quarter.

Year	QOC's	ISO Standard
2012	38	2008
2013	39	2008
2014	38	2008
2015	38	2008
2016	38	2008
2017	40	2015

In 2017, the new information structure of QOCs is implemented, with a total of 40 at year-end.

Human Capital Development

Detection of talent and gender equality

Nafin has a human capital management model based on the development of competencies and permanent evaluation of staff's potential. This allowed coverage of 59.1% vacancies with personnel developed within Nafin during January-December 2017, reducing recruitment costs and optimizing investments. Likewise, vacancy coverage was made in support of public policies on government programs to promote gender equality, granting women 40% of promotions during 2017.

Nafin has a program to develop young talents, through professional practices and

social service. As a result, 28 people were hired permanently, which represents 23.5% of hiring made during 2017.

Also, with the firm intention of strengthening the detection of talent, in 2017 there is continuity with online services, which allows identifying external and internal personnel with competencies required for performance of their position, as well as vacancies generated, through a methodology that aligns staff needs with those of Nafin through the generation of a development model by competencies, identification of talent, definition of key positions and their replacements, establishment of an individual development plan as well as the operation of internal coverage of vacant positions.

In 2017, 100% of actions related to Nafin Culture Program on Gender Equality were implemented as well as our Ethics Committee.

Priority training programs

In January-December 2017, our Training Program focused on technical and specialized training, teaching more than 100 internal courses, accumulating a total of 17,637 man-hours of training. This includes our Business English Program, with a scope of 109 benefited employees.

In addition, various actions were carried out to benefit as many employees as possible, such as the teaching of two graduates in Corporate Finance and Risk Management in Financial Institutions, aimed at officials and employees. Likewise, a specialized training for our Regional Promotion Network was continued, through an online diploma course under the name Management Skills and Sales.

As part of our scholarship program, eight scholarships were awarded to employees of Nafin for bachelor and master's degree studies. Likewise, it continues to certify personnel of areas that, by regulation, are required.

Internal Comptroller's Office

Internal control

Compliance with 2017 Work Program

In accordance with our Work Plan for Evaluation of Effectiveness of Internal Control, 36 on-site verifications of various process control tools were carried out, verifying their effectiveness when comparing documentary and electronic evidence generated from each process. Internal Comptroller (DCI) informed Audit Committee about the results of visits.

Internal Control System

At 2017 end, the universe of self-control tools is integrated as follows:

- 34 Corporate Control Guides (GCC).
- 282 Control Routine Agendas (ARC).
- 41 Control Routine Agendas through which the delivery in time and form of 322 Regulatory Reports is monitored.

Heads of administrative units appointed public servants responsible for attending in a timely manner ARCs of processes under their charge, which allow staff to ensure adequate performance of their activities, controlling and mitigating risks inherent to their functions.

Application of Corporate Control Guide (GCC)

During November 2017, GCCs were reviewed and redesigned based on five Internal Control

Standard	Principle	Self appraisal
Control Environment	1. Integrity, Ethics and Values	99%
	2. Supervision of Internal Control	98%
	3. Structure, authority and responsibility	92%
	4. Commitment to retain competent personnel	93%
	5. Compliance with Responsibility	96%
Risk Management	6. Specific Objectives	95%
	7. Identification and Risk Management	97%
	8. Corruption Risk Assessment	87%
	9. Identify significant changes	89%
Control Activities	10. Control activities to mitigate risks	96%
	11. Controls in TIC according to institutional objectives	96%
	12. SGC Policies and Procedures	92%
Information and Communication	13. Relevant information in C.I.	97%
	14. Internal Communication in C.I.	96%
	15. External Communication	96%
Supervision, Monitoring and Continuous Improvement	16. On-the-fly and separate C.I. assessments	94%
	17. Report of incidents and follow-up	75%
Average		93%

standards and their related principles, using a model proposed by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). These guidelines were applied to 100% of holders of 34 administrative units that make up Nafin structure, with the purpose of carrying out annual self-assessments of internal control infrastructure, whose result, as an Internal Control rule, is detailed on the previous page.

Nafin Annual Report of the State that Keeps her Internal Control System for 2017 was presented to Audit Committee and Board of Directors, prior to its presentation to the head of the Ministry of Public Function on January 31, 2018, in compliance to the AGREEMENT by which Provisions and the Administrative Manual of General Application in matters of Internal Control are issued.

Update of objectives and guidelines of Nafin Internal Control Model

On October 27, 2017, Nafin Audit Committee became aware of updating of Objectives and Guidelines of Institutional Model of Internal Control 2017 (LIMICI) and recommended its implementation for the approval of the Board of Directors. Changes to highlight are:

- I. Recognition of the Agreement by which Provisions and the Administrative Manual of General Application in matters of Internal Control are issued, for which articles referenced to said Provision are updated.
- II. It specifies that administrative units are responsible within the scope of their attributions regarding application and

supervision of normative and internal control instruments established, according to particular circumstances of each one of them.

- III. It includes implementation of ISO 9001: 2015 Standard, the basis of Nafin Quality Management System.
- IV. Update of Chapter II “Powers and Responsibilities” of administrative units.

Update of Control Tools

Processes were permanently monitored by control tools under supervision of administrative unit heads, modifying and incorporating reactivities with the following purposes:

- Verify fulfillment of activities that make up critical processes and effectiveness of controls registered in internal control tools.
- Design and/or update control tools according to the needs of the process.
- Jointly implement internal controls to avoid materialization of possible risks.

Regulatory Reports and Reports to Authorities

Among DCI activities is monitoring of timely compliance according to regulations regarding information, preparation and delivery to authorities of various reports requested to Nafin. Internal Comptroller’s Office updated inventory of reports and information requirements, which is housed in the Internal Control Administration System (SACI) to, in this way, promote timely compliance at institutional level. At the close of fiscal year 2017, there is an inventory of 322 regulatory reports requested to Nafin by SHCP, CNBV and Banxico, among others.

Supervision of compliance with provisions on investment services

DCI, as responsible for overseeing compliance with General Provisions applicable to financial entities and other entities that provide investment services within Nafin, prepared the corresponding reports, which results were reported to the Audit Committee and Board of Directors, and made known to CNBV in a timely manner.

Observations and areas of opportunity for fiscal audits

With respect to observations determined in 2016, our Internal Audit Division reviewed the same during the third quarter of 2017. For the closing of fiscal year, said entity carried out the 12/2017 audit, determining two findings related to improvement proposals to SACI, referring to the role and attributions of a consultant who administers said system, as well as carrying out activities aimed at eliminating recurrence of amber alerts generated by said system, so that to date they are in the process of attention.

Reports generated by Internal Comptroller Office

This Office is in charge of preparing reports in accordance with applicable regulations for delivery to various authorities. During 2017, six regulatory reports on internal control were prepared, according to the following periods:

- Five reports on deviations from current credit objectives, guidelines, policies, procedures, strategies and regulations (annually and quarterly to Risk Management Committee, Audit Committee and Board of Directors)

- Two reports on supervision of compliance with Provisions on Investment Services from July to December 2016. (Semi-annually to Audit Committee, Board of Directors, Financial Products Committee and Mexican Banking and Securities Commission (CNBV))
- Four Regulatory Reports R27-B 2711 Stocks Claims (quarterly to Audit Committee and Board of Directors)
- A report on performance of activities as well as Internal Control System operation (Audit Committee and Board of Directors)
- An annual report of state kept by Nafin Internal Control System (General Direction, Audit Committee, Board of Directors and Ministry of Public Function)
- A report on inactive accounts in accordance with Art. 61 of the Law on Credit Institutions (Annually CNBV and Public Welfare)

Prevention of Operations with Resources of Illicit Origin and Combat the Financing of Terrorism

Design and development of an Illicit Operations Prevention Model with a risk-based approach

Due to the Resolution that amends, adds and repeals various provisions of a general nature referred to in article 115 of Credit Institutions Act, published by SHCP on February 24, 2017, and in order to comply with provisions of Chapter II Bis "Risk Based Approach", our Compliance Office initiated processes for hiring of an independent expert advisor, in order to design and develop a methodology for prevention and identification of operations with resources of illicit origin with an approach focused on risk for Nafin.

The firm Traces Corporate Consulting, S.C. was contracted through a direct award. Works for the design and conceptual development of an Illicit Operations Prevention Model with an Approach Focused on Risk (PLD-EBR Model), began on November 10, 2017.

The methodology that groups together different documents and risk matrices was concluded on December 5 and presented to our Communication and Control Committee (CCC) during the 12th/2017 ordinary session, corresponding to December 2017, with a favorable opinion of its members.

Preventive processes of illicit operations

466 applications were attended to determine level of risk, from 12 divisions (Promotion of Markets, Productive Chains, Fiduciary, Corporate Finance, Financial Intermediaries and Microcredit, Sustainable Projects, Human Resources and Quality, Financial Markets, Network Coordination, International Financial Organizations, Treasury, as well as the Legal Area of Banking Formalization).

With respect to formats part of prevention processes of illicit operations, 554 formats were attended: 332 of Identification and Knowledge of Your Customer or User (FICC); 29 Appendices of FICC, 82 of Verification of Politically Exposed Persons (FVPPE), 51 of Accounts Registration, Deletion and Changes or Registration, Deletion and Changes and Derivatives; 15 of Identification and Knowledge of your Customer with Fiduciary Operations (FICC-FISO), and 45 of Declaration of Probity, in which not only the corresponding risk rating is issued, but it is also documented evidence of each customer and its shareholders, legal attorneys and persons authorized to enter into transactions.

Technological Developments in Monitoring System

Regarding technological developments for a System of Relevant and Unusual Operations

(SORI), three projects were concluded, which are mentioned below.

The first is related to restoration of connection between Fiduciary and Accounting Information System (SIFC) and Human Resources System (LOBO) with SORI, in order to extract from them basic information to perform monitoring functions and follow-up of operations.

The second refers to data association of people related to the same Federal Taxpayer Registry (RFC) of customers. This development was concluded and released in August 2017. Its main objective is to register data of authorized third parties, co-owners, real owners, resource providers, beneficiaries, users, legal representatives and attorneys related to customer's RFC, and that these can be selected, replicated and associated with contracts already captured from the same customer in SORI customer base.

In December, contract data association to SORI customer records was concluded, which aims to relate contracts of customers and transactional profiles corresponding to each contract number.

Compliance of information exchange between banks and with authorities regarding prevention of illicit operations

To comply with the 62nd Quarter of General Dispositions referred to in article 115 of Credit Institutions Law, which deals with guidelines for exchange of information between credit institutions and competent authorities, Banxico made available to all banks a technological development called Cross-Border Transfers Database (BDTT). However, for its use, support of IT Division was required

in order to develop a statistical information query application of BDTT, under technical specifications given by Banxico.

Process to comply with FATCA

DCI, through the Compliance Office as responsible for coordinating Nafin actions in order to comply with bi-national agreements related to Foreign Account Tax Compliance Act (FATCA), as well as Common Reporting Standard (CRS), since March, it has taken actions regarding identification of customers that qualify as Specific Persons of the United States of America.

With the support of SKATT, Asesores Fiscales, S.C., it was concluded with the background and evidence review of 102 records of corporate customers of our Market Promotion Division and 97 of our Trusts Division, in order to find indications that would allow a sustained decision to be made and under criteria established to report or exclude customers, as it corresponds to the criteria established by the US Department of Treasury, through the Internal Revenue Service (IRS), in the case of FATCA processes, and selection and reporting criteria of customers reviewed for CRS, established by OECD, through bilateral agreements signed by SHCP with different governments in the area of cooperation in the exchange of information on taxation and prevention of international tax evasion.

Likewise, with information collected from review of files, and Self-Certification Formats that business areas received from their customers, the corresponding reports were prepared for the Mexican Internal Revenue Service (SAT), sending 16 files in total, obtaining

the corresponding acknowledgments of receipt as evidence of Nafin compliance.

For FATCA processes, two were sent to customers of Trust Fund for the Sale of Direct CD to the Public (Cetesdirecto) and two by customers of our Fiduciary Division. In the case of CRS processes, 12 corresponding files were sent to people to report.

From trusts in which documentary evidence was found not containing any physical person under the category of Specific Person of the USA or for CRS guidelines, 384 files were prepared and delivered to SAT, about trusts that do not have reportable information.

With the support of SKATT firm, a specialized training program was carried out for a total of 27 participants, including employees and officials from areas involved in compliance process of FATCA and CRS. In addition, the first version of an Institutional Guide for consultation regarding related processes was prepared.

Program of identification files and knowledge of customers with high risk rating

During November, 20 cases were verified in the divisions of Market Promotion, Fiduciary, Corporate Financing, Financial Brokers and Microcredit, and Productive Chains. The result was very favorable, since it was found that areas comply with applicable regulations and with Internal Manual for the Prevention of Money Laundering (PLD).

Sending official reports to authorities

During fiscal year 2017, the following reports were sent:

- Four reports of Relevant Operations
- Four reports of Operations with Dollars in Cash
- Four reports of Operations with Cashiers' Checks
- 12 reports of International Fund Transfers
- 12 reports R29-A2911 assurances, transfers and unblocking of accounts
- An Audit Report (annual conducted in March)
- A Report on Integration of the Communication and Control Committee
- A Report on results of Training Program

Regarding reports of Unusual Operations, Worried Internal Operations and Unusual Operations 24 hours, no operation was presented under those circumstances.

Requirements of authorities via CNBV

In order to maintain business lines with foreign counterparts, 27 applications were answered, which refer to six Wolfsberg Questionnaire formats, eight Anti-Money Laundering Questionnaires from Bank of Montreal, Citibanamex, HSBC Canada, Santander, Société Générale, Nomura London, Credit Suisse, Bladex, Mizuho, Barclays Barclays and Morgan Stanley. Likewise, eight requests for Due Diligence were answered, in which they requested general information from Nafin, such as Board of Directors, Financial Statements in English, identifications of Board of Directors members; two requirements with respect to due compliance with FATCA law, two of Due Comprehensive Diligence, named Call Reports, and a questionnaire for CIMA (Cayman Islands Monetary Authority).

Support for administrative transition in Nafin Branch in London, United Kingdom

In the process of management change and ad-

ministrative restructuring in Nafin Branch in London, United Kingdom, during the second semester of 2017, our Compliance Office provided support to inform current executives about compliance processes in matters of prevention of operations with resources of illicit origin and combating the financing of terrorism. This for responding to due diligence processes required by European and North American banks with whom they carry out operations.

Also, while new managers and officials carried out procedures to obtain necessary certifications, which according to regulations in the United Kingdom in the prevention of money laundering they had to obtain, our Compliance Officer carried out a temporary compliance requesting attention to requests and necessary responses to foreign banks, so that said branch would keep its business channels open, avoiding operating closure due to lack of compliance with said banking entities.

Nafin Branch in Grand Cayman, Cayman Islands

Monetary Authorities of the Cayman Islands (CIMA) published regulations related to compliance processes in matters of money laundering prevention and combating the financing of terrorism. With this change, the representation agent Cainvest Bank and Trust, LTD. informed Nafin about the creation of an electronic compliance portal called REEFS (Regulatory Enhanced Electronic Forms Submission). In December, our Compliance Office completed the first compliance phase on said portal, registering a general administrator of the portal for Nafin and waiting for new indications from authorities of that country.

Training Program in Prevention of Money Laundering and Fight against Terrorist Financing

In September 2017, contracting processes of a specialized service in e-learning courses for the design and development of a Training Program in the area of Prevention of Money Laundering and Terrorist Financing were concluded. The provider of the winning service delivered materials and access to this online course on its own technological platform. Likewise, contents of training were prepared according to guidelines and requirements that DCI requested and, once developed, reviewed for approval.

Training Program in Prevention of Money Laundering and fight against Terrorist Financing considered a training period of four weeks, from October 16 to November 10, in which all Nafin active personnel participated (employees and officials), with the exception of personnel working in the kitchen, drivers and auxiliary security personnel. A total of 981 participants were registered, in two types of courses, according to their tasks:

- General course: 588 participants
- Advanced course: 393 participants

This Training Program results were presented to the Communication and Control Committee, in the 11th/2017 ordinary session held during November.

Also, this program worked in coordination with our Social Communication Division for a campaign among staff, which included designs and contents for posters, roll-ups and informative emails.

Internal Auditing

Our Internal Audit Division (DAI) prepared and attended its Annual Work Program 2017, which was oriented to auditing Nafin main activities, highlighting those related to credit, financial markets, trusts and risk management, in which, in general terms, had the objective of verifying compliance with regulations, among others that established by CNBV and Banxico; evaluate quality, sufficiency and timeliness of financial information; verify administration of risks inherent in processes, and strengthen our Internal Control System.

In accordance with the above, activities of DAI covered the following aspects.

1. Audits

15 audits were carried out, of which six were normative, according to the following: i) four to Credit Process, ii) one to Risk Management, in compliance with provisions issued by CNBV, and iii) one to operation of Financial Instruments-Derivatives, in accordance with Banxico standard; the remaining nine are integrated as follows: one to Financial Agent-Front Office, Regulatory Reports-CNBV, Financial Statements, Money Market, one to a trust and four follow-ups.

During reviews, audited areas were contacted in order to inform people in charge about the results and proposals with added value that would allow them to take care of observations, as well as recommendations determined in order to strengthen our Internal Control System.

2.- Audit Committee (CA)

Our Internal Audit Division supports activities of an Audit Committee, among which it is

important to provide necessary elements to inform the Board of Directors about the situation of the Internal Control System, as well as logistics of sessions, obtaining information for its development and follow-up of agreements. In 2017, 10 ordinary and two extraordinary sessions were held.

3.- Participation as normative advisors in sessions of decision-making entities (committees)

In compliance with legal provisions, we participated in sessions held by Integral Risk Management Committee and Communication and Control Committee. In addition, Executive Credit Committee of the Board of Directors, Internal Credit Committee and Credit Committee were involved.

4. Monthly review of variations in Nafin Financial Statements

With the purpose of evaluating the reasonableness of figures in the General Balance and Profit and Loss Statement, on a monthly basis items showing the main variations are identified, making comparison of balances of financial information from the previous month against preliminary figures registered in Financial Information System of the month, determining increments and decreases of balances and analyzing their origin.

Likewise, DAI participated quarterly in the working group with members of Audit Committee and representatives of our Administration Division, with the purpose of carrying out the analysis of information in the Financial Statements and, if applicable, explanations and/or clarifications were made.

5. Internal Audit Process Operating Manual

In the second semester of 2017 this Manual was finished, including the following activities: Analysis of Variations in Financial Statements, Comments on Request of Credit Committees and Guarantees; Participation in Allocation of Resources through Auctions to FIs that collaborate in Guarantees Program, Review of Cases of Credit Punishment, Audit Committee, Preparation of Reports and Activities in Charge of Audit Committee and Preparation of a Follow-up Report to Observations in the Process of Attention.

6. Audit Management System

During 2017, together with our IT Division, use cases were reviewed, where technical details derived from concept analysis of functionalities required to systematize tasks executed by our Internal Audit Division were carried out. At 2017 end, the review of 35 (47%) use cases out of 73 has been completed.

IT

- Continuous Improvement in Operation
 - » **Certification of Primary Data Center**
In order to certify our Primary Data Center in level III of International Computer Room Experts Association (ICREA) standard, adjustments were made to reinforce safety measures in physical environments, as well as renewal of electrical wiring and telecommunications. This was carried out with great precision without any impact on the operation of business areas. With these actions, operation

of Nafin Data Center is feasible for the next 15 years and it is possible to position it at the same level of certification as our Alternate Data Center.

» **Technological Update of Distributed Infrastructure**

The project consisted in installation of 13 physical servers, 80 virtual servers, two storage systems and two tape backup and recovery systems, with state-of-the-art technology, migrating to infrastructure services and collaboration tools such as electronic mail, unified communications, active directory, perimeter security, etc., also increasing the storage of digital information by 15%.

▪ **Developments-Applications**

- » During 2017, 30 business projects were implemented, of which 13 were implemented through contracting and administration of external suppliers according to current regulations; two, through a combination of internal developments and contracting and administration of external suppliers; and 15 through internal developments that allowed Nafin to generate significant savings, with the benefit of not generating dependency with a sole supplier. It is important to mention that

this strategy allows knowledge and experience to remain in Nafin and reduces response time to meet business needs, supporting professional growth of participants in these projects. Of the internal developments that were implemented this year, the following projects stand out: Version 17.0 of the nafin.com Institutional Portal, estimated in six months and the entire project was developed with internal resources from our IT Division, ending on schedule and in accordance with plan, with savings for Nafin.

» **Ver. 16.0 Maintenance SIDECAMW**

This project was developed with internal resources, to comply with regulatory requirements of modifications issued by regulatory bodies for the administration of Swaps of TIIE settled in ASIGNA through settlement partners in the front and middle office processes, as well as registration accountant, since the proposal of our previous supplier did not comply 100% with the requirements. In case of having contracted this development Nafin would have generated expenditures for 7 million pesos plus an annual maintenance cost and dependency with provider. ¶



FINANCIAL RESULTS

Despite an environment of volatility and decline in economic activity, in 2017 Nafin obtained a net profit of 1.502 billion pesos, equivalent to a return on capital of 5.3% at nominal terms. As a result, stockholders' equity reached a balance at the end of the year of 31.444 billion pesos, which represented a nominal growth of 17.7% compared to 2016. It is worth mentioning that in this year the Federal Government used resources from Nafin for 550 million pesos, so without this use the net profit would have been 1832 million pesos and the return on capital of 6.5%.

Additionally, Nafin's financial situation shows solid indicators, such as the following:

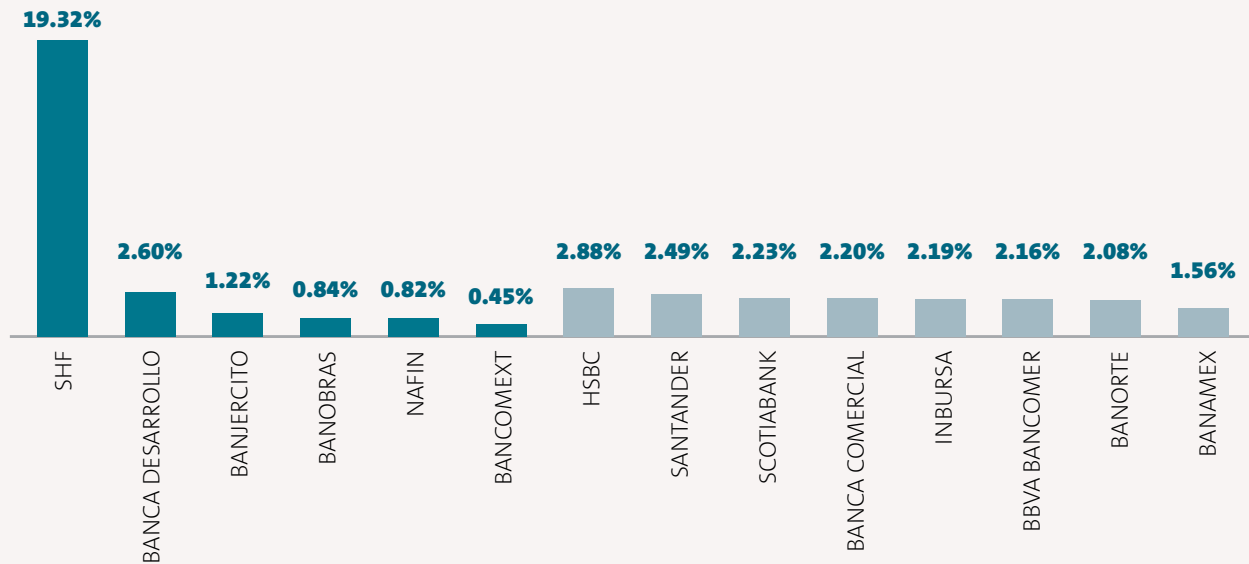


Indicator	Dec. 2016	Dec. 2017
Past due portfolio / risk portfolio	1.1%	0.9%
Reserves / past due portfolio	205.0%	241.6%
Financing granted to MSMEs/Financing to Private Sector	76.8%	76.8%
Financial Penetration (Private Sector Portfolio/GDP) 1/	1.8%	1.7%
Financial Penetration (Private Sector Portfolio and Capital Contribution/GDP) 1/	2.1%	2.1%
Return on Equity (ROE) 2/	5.2%	5.3%

1/ Mexican GDP for December 2017 estimated with December 2016, annual GDP growth of 1.49% and annual inflation of 6.77%. It is worth mentioning that GDP data has been revised upwards by INEGI having incorporated technological information and communication activities (TIC's).

2/ It considers Federal Government uses for 800 and 550 million pesos in 2016 and 2017, respectively.

Banking System Past-Due Portfolio



Evolution of past due loans with risk

The 2017 Operating and Financial Program considered keeping loan indicators low and, if possible, reducing past due loan portfolio at risk.

At the end of December 2017, loan portfolio recorded in the balance sheet was 228.395 billion pesos. Past due portfolio with risk, at the end of 2017 was 1867 million pesos, mainly concentrated in portfolios of Financial Intermediaries Mod. "B" with 1.284 billion pesos (69%), Programs with 575 million pesos (30.6%) and Former Employed 8 million pesos (0.4%).

Comparison with Other Banks

Past Due Loan Index (ICV) of 0.82% reached in December 2017, places Nafin below Banjercito

(Bank of Mexican Army, Air Force and Navy) and Banobras and above Bancomext. Sociedad Hipotecaria Federal (SHF) presents the highest ICV of development banks with 19.32%.

Also, Nafin compares favorably against 2.20% of commercial banks, as well as with the main commercial banks: HSBC, Santander, Scotiabank, Inbursa, BBVA Bancomer, Banorte and Banamex.

Portfolios of Programs, Banks and Modality "A", FI Public Sector and Decentralized Entities that make up 47.89% of total portfolio with risk, remain without past due portfolio.

With the exception of a trust that supports Housing Development and the first-floor credit reported as of December 2017, levels of nonperforming loans have been contained. The foregoing considering continuity of planned strategies, among which are:

- Issuance of early warnings, derived from supervision and follow-up visits to portfolio of first and second floors, which favor timely decision making.
- Immediate and direct extrajudicial collection, attending payment proposals or credit restructurings, where appropriate, for authorization of authorized bodies.
- Better control of past due portfolio, through a Recovery and Monitoring System.
- Application of preventive reserves and credit penalties, in accordance with Nafin regulations authorized by the Board of Directors.
- Training of personnel responsible for supervision, monitoring and recovery, in order to increase their knowledge and skills directly related.

In accordance with the foregoing, Nafin has a team of executives specialized in supervision and monitoring of loan portfolio and guarantees, as well as in extrajudicial collection, and we continue with maintenance, development and adjustments to Nafin supervision and recovery systems, in order to have more efficient tools for monitoring and

controlling portfolios, which allow monitoring of compliance with regulations by financial intermediaries and accredited.

Balance Sheet

As of December 2017, Nafin's assets amounted to 529.082 billion pesos, financed with liabilities of 497.638 billion pesos, which, in turn, are comprised of 188.768 billion pesos of creditors by repurchase agreement, 214.351 billion pesos of domestic debt and 94,520 million pesos of external debt and other liabilities.

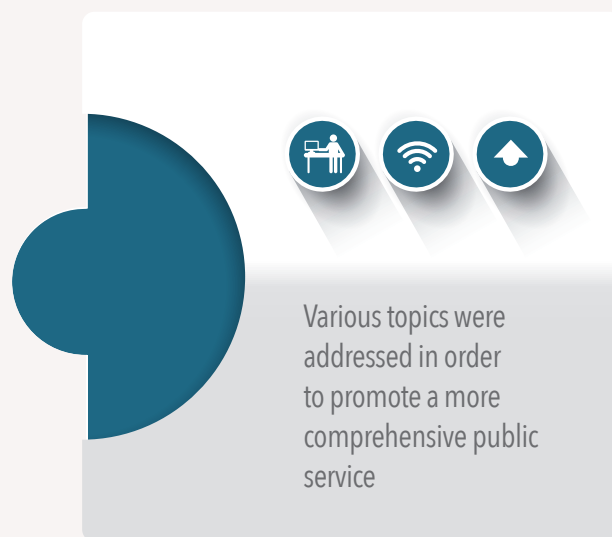
In addition, a balance as Financial Agent balance was recorded in memorandum accounts for 368.960 billion pesos, which grew by 4.589 billion pesos in 2017, equivalent to 1.3%. Also, a contingent balance of guarantees was reached for 72.558 billion pesos, observing an increase of 14.2% with respect to 2016 balance, due to dynamism and acceptance of Nafin Guarantee Program.

The analysis of Nafin Financial Statements for the 2017 period is reported in "Appendix B.- Report on Consolidated Financial Statements with Subsidiaries as of December 31, 2017", of this report. ¶



INTERNAL CONTROL

- **During 2017**, Nafin Internal Control Entity (OIC) carried out its activities in accordance with powers provided for in Articles 98 and 99 of SFP Internal Regulations, as well as Article 44 Bis 1 of the Law on Credit Institutions that, from 2014 Financial Reform, it allows to carry out control, evaluation and monitoring of administrative provisions applicable to the institutions of development banking on 1) budget and fiscal responsibility; 2) acquisitions, leases and services of public sector, public works and related services; 3) conservation, use, destiny, affectation, alienation and loss of goods; 4) administrative responsibilities of public servants, and 5) transparency and access to public information.
- In this sense, OIC Annual Work Plan was prepared and executed based on General Guidelines issued by SFP, focusing actions on four fundamental axes: audit, control and evaluation; legality; modernization and development of management; as well as optimization of resources and cross-application aspects.
- In terms of audit, control and evaluation, planning, programming and execution actions of eight audits were developed, as



well as follow-up on certain observations, adopting measures aimed at Nafin strengthening and fulfillment of objectives and goals, with criteria of economy, effectiveness, efficiency, impartiality, honesty and adherence to regulations, privileging the prevention of corruption and administrative offenses, as well as to improve performance of internal control.

- Regarding the axis of legality, OIC carried out activities in the area of complaints and denunciations investigation for possible non-compliance with obligations of federal public servants and those persons who handle or apply federal public

resources, as well as complaints related to infractions of individuals or companies due to their participation in public federal acquisitions.

- Based on the General Law of Administrative Responsibilities and in accordance with provisions of article 115, an authority in charge of administrative liability procedures must be different from the one in charge of such investigation. In that sense, OIC modified its structure to have an Area of Responsibilities and another of Complaints, which carry out their functions independently.
- Regarding management modernization and development, actions were carried out aimed at the standardization of processes, regulatory improvement, organizational and occupational structures alignment towards strategic

objectives, professionalization, planning and control of human resources and the use of information and communication technologies.

- Likewise, various topics were addressed in a cross-cutting manner in order to promote a more comprehensive public service, among others, those related to transparency and accountability, citizen participation, ethics and prevention of possible conflicts of interest.
- In accordance with the above, OIC helped to maintain Nafin internal control system, supporting decision-making processes for fulfillment of goals and objectives, achievement of the National Development Plan, optimal performance of public servants, modernization and efficient development of management and correct use of public resources. ¶

EXHIBIT A

NAFIN RELEVANT FIGURES

TABLE 1

NACIONAL FINANCIERA, S.N.C., RELEVANT FIGURES

Millions of MXN to End of Year

Concept	2014	2015	2016	2017
Total Assets 1/	389,750	384,828	503,541	516,230
Financing Agent Portfolio	1,013	109	94	65
Commercial Banks (First-tier) Portfolio	32,926	43,730	66,299	63,004
Second-tier Banks Portfolio	<u>116,360</u>	<u>127,863</u>	<u>147,920</u>	<u>165,390</u>
Total Credit Portfolio	150,299	171,702	214,313	228,459
Equity Investment in Companies	5,740	6,514	8,010	8,952
Equity Investment in Real Estate Companies	1,496	1,532	1,539	1,637
Equity Investment in Stock	23	95	59	269
Internal Debt	156,019	184,342	213,222	214,351
External Debt	31,327	44,054	63,533	71,927
Previous Reserves for credit risks	3,665	3,999	4,464	4,511
Total liabilities	376,342	371,062	488,365	497,638
Stockholders' Equity	22,942	24,096	26,710	31,444
Assets in a Trust or Agency	1,325,455	1,403,376	1,544,545	1,725,173
Debtor by Guarantee and Other Contingent Liability	56,359	64,414	53,520	235,458
Net Profit (Loss)	1,648	1,254	1,321	1,502
Compounding Level (%)	15	14	13	14

1/ Consolidated with Subsidiaries

TABLE 2

**Operation for Promotion of Private Sector
By Second-tier, First-tier and Guarantees
Regional Classification**

(Millions of Mexican Pesos - Number of Companies)

Credit and Collateral Jan-Dec 2016			Credit and Collateral Jan-Dec 2017		Percentage Variation 2017/2016	
Amount	Company		Amount	Company	Amount	Company
550,789	715,741	TOTAL	546,534	565,531	(0.8)	(21.0)
29,388	42,990	NORTHWEST	28,882	33,204	(1.7)	(22.8)
9,139	17,393	Baja California	9,165	12,109	0.3	(30.4)
1,783	5,946	Baja California Sur	1,698	1,800	(4.8)	(69.7)
10,721	6,430	Sinaloa	9,742	5,386	(9.1)	(16.2)
7,745	13,221	Sonora	8,277	13,909	6.9	5.2
105,964	108,201	NORTHEAST	100,969	73,473	(4.7)	(32.1)
14,531	17,785	Coahuila	12,662	13,760	(12.9)	(22.6)
11,056	8,376	Chihuahua	10,581	9,373	(4.3)	11.9
3,925	13,421	Durango	3,903	5,274	(0.6)	(60.7)
66,599	39,223	Nuevo León	66,254	27,503	(0.5)	(29.9)
9,853	29,396	Tamaulipas	7,569	17,563	(23.2)	(40.3)
89,181	126,723	CENTER WEST	85,985	108,684	(3.6)	(14.2)
4,831	6,313	Aguascalientes	4,486	3,655	(7.1)	(42.1)
5,241	3,462	Colima	3,122	3,068	(40.4)	(11.4)
14,794	18,007	Guanajuato	16,993	16,139	14.9	(10.4)
41,261	27,987	Jalisco	40,110	28,925	(2.8)	3.4
8,729	30,186	Michoacán	8,091	19,889	(7.3)	(34.1)
1,852	5,133	Nayarit	1,734	3,156	(6.4)	(38.5)
9,378	29,403	San Luis Potosí	8,666	27,669	(7.6)	(5.9)
3,094	6,232	Zacatecas	2,782	6,183	(10.1)	(0.8)
280,679	290,908	CENTER	290,194	223,965	3.4	(23.0)
183,261	88,029	Mexico City	202,803	62,125	10.7	(29.4)
2,946	32,596	Guerrero	2,352	13,174	(20.2)	(59.6)
6,614	14,064	Hidalgo	6,713	16,093	1.5	14.4
52,322	77,039	State of Mexico	51,082	69,367	(2.4)	(10.0)
7,430	19,518	Morelos	3,797	20,059	(48.9)	2.8
8,720	9,220	Querétaro	8,571	6,452	(1.7)	(30.0)
17,894	43,764	Puebla	13,725	29,273	(23.3)	(33.1)
1,492	6,678	Tlaxcala	1,151	7,422	(22.8)	11.1
45,577	146,919	SOUTH-SOUTHEAST	40,504	126,205	(11.1)	(14.1)
5,242	10,078	Campeche	3,248	10,970	(38.0)	8.9
4,516	16,697	Chiapas	4,707	24,517	4.2	46.8
3,053	15,960	Oaxaca	3,096	8,474	1.4	(46.9)
3,594	11,745	Quintana Roo	4,009	16,011	11.6	36.3
5,740	13,877	Tabasco	5,663	6,825	(1.3)	(50.8)
17,329	64,168	Veracruz	13,512	48,685	(22.0)	(24.1)
6,103	14,394	Yucatán	6,269	10,723	2.7	(25.5)

TABLE 3

DEPOSITS IN MEXICAN PESOS*
(Millions of MXN)

Instrument	2014	2015	2016	2017
Stock Exchange Certificates	28,425	40,000	50,524	56,698
PG's Nafin	<u>111,837</u>	<u>87,587</u>	<u>108,970</u>	<u>79,575</u>
New Instruments	140,262	127,587	159,494	136,274
Term Deposits in Pesos	7,153	41,153	7,153	5,153
Several Deposits	521	8	1,129	1,505
TOTAL	<u>147,935</u>	<u>168,747</u>	<u>167,775</u>	<u>142,932</u>

* Interests not included

TABLE 4

**TOTAL EXTERNAL DEBT
BALANCE AS OF DECEMBER 31**

(Millions of US Dollars)

Concept	2014	2015	2016	2017
I. Direct Debt	<u>2,123.9</u>	<u>2,550.2</u>	<u>3,076.3</u>	<u>3,652.3</u>
A. Deposit Certificates (London)	1259	1140	1387	2067
Euro Promisory Notes	-	-	-	-
Deposit Certificates (London)	1259	1140	1387	2067
B. Green Bonus	-	500	500	500
C. Yen Bonus	-	-	-	222
D. Multilateral Organizations	68	6	5	3
E. Private Banking, Eximbanks and Suppliers	797	904	1184	860
Accrued Interest	<u>1</u>	<u>4</u>	<u>5</u>	<u>6</u>
II. Total Guaranteed Debt	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Total	<u>2,125.1</u>	<u>2,554.0</u>	<u>3,081.2</u>	<u>3,658.0</u>



EXHIBIT B

REPORT ON CONSOLIDATED FINANCIAL
STATEMENTS WITH SUBSIDIARIES
AS OF DECEMBER 31, 2017



Nacional Financiera, S. N. C.
Institución de Banca de Desarrollo
and Subsidiaries

Consolidated Financial Statements

December 31, 2017

(With comparative figures at December 31, 2016)

(With the Independent Auditors' Report Thereon)

(Translation from Spanish Language Original)



KPMG Cárdenas Dosal, S.C.
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INDEPENDENT AUDITOR'S REPORT

The Board of Directors:

Nacional Financiera, S. N. C.

Institución de Banca de Desarrollo

(Millions of Mexican pesos)

Opinion

We have audited the consolidated financial statements of Nacional Financiera, S. N. C., Institución de Banca de Desarrollo and subsidiaries (the Institution) which comprise the consolidated balance sheets as of December 31, 2017, and the consolidated statements of income, changes in stockholders' equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

In our opinion, the accompanying consolidated financial statements of the Institution, have been prepared, in all material respects, in accordance with Accounting Criteria for Credit Institutions in Mexico (the Accounting Criteria), issued by the National Banking and Securities Commission (The Banking Commission).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the "Auditors' responsibilities for the audit of the consolidated financial statements" section of our report. We are independent of the Institution in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Mexico, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole and in forming our opinion thereon, and we do not provide a separate opinion on these matters

(Continued)

Aguascalientes, Ags.
 Cancún, Q. Roo.
 Ciudad de México.
 Ciudad Juárez, Chih.
 Culiacán, Sin.
 Chihuahua, Chih.

Guadalajara, Jal.
 Hermosillo, Son.
 León, Gto.
 Mérida, Yuc.
 Mexicali, B.C.
 Monterrey, N.L.

Puebla, Pue.
 Querétaro, Qro.
 Reynosa, Tamps.
 Saltillo, Coah.
 San Luis Potosí, S.L.P.
 Tijuana, B.C.



Derivative financial instruments \$1,885 asset and \$7,785 liability and valuation adjustment from hedging on financial assets \$15,294 and valuation adjustment from hedging on financial liabilities \$11,203	
See note 9 to the consolidated financial statements	
Key audit matter	How the key audit matter was addressed in our audit
<p>The fair value determination, at the consolidated balance sheet date, of derivative financial instruments non-listed on recognized markets and hedging transactions is carried out through the use of valuation techniques that involve a high degree of judgment by the Management, mainly when it is required the use of inputs obtained from different sources. In addition, the requirements that must be met for accounting for financial instruments classified as hedges, as well as documentation and monitoring to prove their effectiveness, involve a high degree of specialization by the Management.</p>	<p>As part of our audit procedures, we obtained evidence from the Institution of the valuation models for derivative financial instruments and hedging operations used by the Management. Likewise, through selective tests, we evaluate the reasonableness of these models and the inputs used, through the participation of our specialists. In addition, through selective testing, we evaluate the fair value determination of the derivative products and for hedging operations, the proper compliance with the criteria and documentation to be considered as such.</p>
Allowance for loan losses \$7,016	
See notes 3(i) and 10(d) of the consolidated financial statements	
Key audit matter	How the key audit matter was addressed in our audit
<p>The allowance for loan losses involves a high degree of judgment for the evaluation of the capacity of payment of the borrowers, considering the different factors established in the methodologies established by the Banking Commission for the credit portfolio rating process, as well as the accuracy in the documentation and its update, which serves as input for the determination of the allowance for loan losses.</p>	<p>The audit procedures applied to management's determination of allowance for loan losses and its effect on the year results included selective tests of both the inputs used and the calculation method for the different loan portfolios based on the current methodologies established by the Banking Commission for each type of loan portfolio.</p>

(Continued)



Calculation of retirement and termination employees' benefits \$306	
See notes 3(s) and 20 to the consolidated financial statements	
Key audit matter	How the key audit matter was addressed in our audit
<p>The Institution has established defined benefit plans for its employees. The determination of the liability related to such plans at the consolidated balance sheet date was made through complex actuarial calculations that require a high degree of judgment in the selection of the assumptions used to determine the net projected liability of the retirement and termination employees' benefits.</p>	<p>We evaluate through the participation of our actuaries the reasonableness of the assumptions used by the Institution's Management to determine the net projected liability of the retirement and termination employees' benefits, and the calculation method used.</p> <p>In addition, selective items were tested to corroborate the adequate incorporation of the personnel data that were included as a basis for the actuarial calculation. Likewise, we verified compliance with accounting records and disclosures in accordance with the provisions of the Banking Commission.</p>

Current income tax (IT) \$344 and deferred IT and employee statutory profit sharing (ESPS) net asset \$1,338	
See notes 3(o) and 21 to the consolidated financial statements	
Key audit matter	How the key audit matter was addressed in our audit
<p>The determination of current and deferred income taxes and ESPS is complex, mainly due to the interpretation of the legislation in force in the matter, requiring a high degree of professional judgment. The valuation of deferred income tax and deferred ESPS assets requires evaluating factors relating to the current and future operations of the Institution to estimate the realization of these assets.</p>	<p>The audit procedures applied to the calculations determined by the Institution's Management for the recognition of current and deferred income taxes and ESPS included selective tests to compare the income and expense concordance against the accounting records, as well as the nature of the items that were part of the calculations, considering the legislation in force in tax matters.</p> <p>Additionally, we evaluate the reasonableness of the tax profit projections determined by the Institution's management that support the probability of the realization of deferred income tax and deferred ESPS assets.</p>

(Continued)



Responsibilities of management and those charged with governance for the consolidated financial statements

Management is responsible for the preparation of the consolidated financial statements in accordance with the Accounting Criteria established by the Banking Commission, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing 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 realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Institution's financial reporting process.

Auditors' responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Institution's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Institution's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Institution to cease to continue as a going concern.

(Continued)



- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Institution to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Institution audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence and we communicate with them all relationships and other matters that may reasonably be thought to bear our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Emphasis of matter – Comparative financial information

We draw attention to note 4 to the consolidated financial statements which indicates that the comparative information presented as at and for the year ended December 31, 2016 has been restated. Our opinion is not modified in respect of this matter.

Other matters

The consolidated financial statements of Nacional Financiera, S. N. C., Institución de Banca de Desarrollo and subsidiaries as at December 31, 2016 and for the year then ended, excluding the restatement adjustments described in note 4, were audited by other auditors who expressed an unmodified opinion on those consolidated financial statements on February 15, 2017.

As part of our audit of the consolidated financial statements as at and for the year ended December 31, 2017, we have audited the restatement adjustments described in note 4 to the consolidated financial statements that were applied to restate the comparative information as at and for the year ended December 31, 2016. We were not engaged to audit, review or apply any audit procedures to the consolidated financial statements of the Institution as at and for the year ended December 31, 2016, other than with respect to the restatement adjustments described in note 4. Accordingly, we do not express an opinion or any other form of assurance on those respective consolidated financial statements taken as a whole. In our opinion the restatement adjustments described in note 4 to the consolidated financial statements are appropriate and have been properly applied.

KPMG Cárdenas Dosal S. C.

Aarón López Ramírez

Mexico City, February 16, 2018.

Nacional Financiera, S. N. C.,
Institución de Banca de Desarrollo
and subsidiaries

Av. Insurgentes Sur 1971, Col. Guadalupe Inn, C.P. 01020, Mexico City

Consolidated Balance Sheet

December 31, 2017

(With comparative figures at December 31, 2016, note 4)

(Millions of Mexican pesos)

Assets	2017	2016 (note 4)	Liabilities and Stockholders' Equity	2017	2016 (note 4)
Cash and cash equivalents (note 6)	\$ 28,551	15,698	Deposit funding:		
Margin accounts	35	-	Time deposits (note 15):		
Investment securities (note 7):			Money market	\$ 134,296	143,470
Trading	194,472	220,261	Debt securities issued:		
Available-for-sale	15,087	13,554	In the country (notes 15 and 16):		
Held-to-maturity	13,545	12,871	Stock certificates	57,595	51,367
	223,104	246,686	Abroad (notes 15 and 17):		
Debtors on repurchase/resell agreements (note 8)	2,718	20	Bank bonds	40,670	28,622
Derivatives (note 9):			Stock notes	14,246	10,352
Trading purposes	1,885	182		246,807	233,811
Valuation adjustment from hedging of financial assets (note 9)	15,294	71	Bank and other borrowings (note 18):		
Current loan portfolio (note 10):			Due on demand	8,006	5,700
Commercial loans:			Short-term	4,810	13,339
Business or commercial activity	51,733	59,882	Long-term	12,585	11,311
Financial entities	158,600	134,329		25,401	30,350
Government entities	16,067	17,688	Creditors on repurchase/resell agreements (note 8)	188,768	202,689
	226,400	211,899	Derivatives (note 9):		
Consumer loans	8	8	Trading purposes	80	51
Residential mortgages loans	119	134	Hedging purposes	7,705	9,504
Loans granted as Federal Government Financial Agent	65	94		7,785	9,555
Total current loan portfolio	226,592	212,135	Valuation adjustments of hedging financial liabilities (note 9)	11,203	(3,699)
Past-due loan portfolio (note 10):			Other accounts payable (notes 19, 20 and 25):		
Commercial loans:			Income tax payable	253	329
Business or commercial activity	575	602	Employee statutory profit sharing payable	275	269
Financial institutions	1,284	1,560	Creditors on settlement of transactions	-	88
	1,859	2,162	Creditors on collateral received in cash	1,109	1,126
Consumer loans	2	4	Sundry creditors and other accounts payable	1,669	1,590
Residential mortgages loans	6	12		3,306	3,402
Total past-due loan portfolio	1,867	2,178	Deferred credits and prepayments	98	40
Loan portfolio (note 10)	228,459	214,313	Total liabilities	483,368	476,148
Less:			Stockholders' equity (note 22):		
Allowance for loan losses (note 10)	(7,016)	(5,639)	Paid-in capital:		
Total loan portfolio, net	221,443	208,674	Capital stock	8,805	8,805
Other accounts receivable, net (note 11)	16,561	25,897	Contribution for future capital increases formalized by the Board of Directors	5,700	2,750
Foreclosed assets, net (note 12)	4	9	Paid stock premium	8,922	8,922
Premises, furniture and equipment, net (note 13)	1,486	1,502	Earned capital:		
Permanent investments (note 14)	2,868	2,890	Statutory reserves	1,730	1,730
Deferred income taxes and employee statutory profit sharing, net (note 21)	1,338	1,021	Retained earnings	4,148	2,795
Other assets:			Result from valuation of available for sale securities	108	(178)
Deferred income charges, prepaid expenses and intangibles	943	1,140	Remeasurements of defined employee benefits (note 20)	(213)	(574)
			Effects of valuation in associate and affiliate companies	742	640
Total assets	\$ 516,230	503,790	Net income	1,502	1,353
			Non-controlling interest	1,418	1,399
			Total stockholders' equity	32,862	27,642
			Total liabilities and stockholders' equity	\$ 516,230	503,790

(Continued)

**Nacional Financiera, S. N. C.,
Institución de Banca de Desarrollo
and Subsidiaries**

Av. Insurgentes Sur 1971, Col. Guadalupe Inn, C.P. 01020, Mexico City

Consolidated Balance Sheet, continued

December 31, 2017

(With comparative figures at December 31, 2016)

(Millions of Mexican Pesos)

Memorandum accounts (note 23)

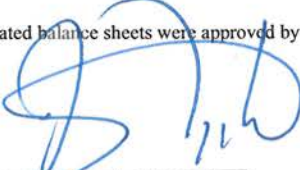
	<u>2017</u>	<u>2016</u>
Guarantees granted	\$ -	72
Contingent assets and liabilities	62,510	53,448
Loan commitments	172,948	135,025
Assets placed in trust or mandate:		
Trusts	1,339,718	1,166,458
Mandates	14,133	13,716
	<u>1,353,851</u>	<u>1,180,174</u>
Federal Government Financial Agent	371,322	364,371
Assets in custody or administration	556,669	593,505
Collateral received by the entity	15,413	22,298
Collateral received and sold or pledged as a guarantee by the entity	12,694	22,277
Investment bank on behalf of third parties, net	42,660	102,943
Interest earned but not collected arising from past-due loan portfolio	168	190
Other memorandum accounts	641,690	610,807

These consolidated balance sheets were prepared in accordance with the Accounting Criteria for credit institutions issued by National Banking and Securities Commission, based on Articles 99, 101, and 102 of the Law for Credit Institutions which are of a general and mandatory nature and have been applied on a consistent basis. Accordingly they reflect the transactions carried out by the Institution through the dates noted above. Furthermore, these transactions were carried out and valued in accordance with sound banking practices and the applicable legal and administrative provisions.

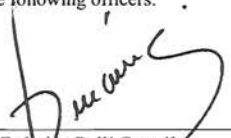
At December 31, 2017 and 2016, the historical capital stock amounts to \$2,390 in both years.

These consolidated balance sheets could be searchable on the following webpage http://www.nafin.com/portalfn/content/nafin-en-cifras/informacion-financiera/estados_financieros.html and <http://portafolioinfo.cnbv.gob.mx/Paginas/contenidos.aspx?ID=37&Titulo=Banca%20de%20Desarrollo>

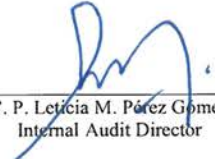
These consolidated balance sheets were approved by the Board of Directors, under the responsibility of the following officers.




Dr. Jacques Rogozinski Schtulman
General Director



Dr. Federico Ballí González
Deputy General Director of Finance and
Administration



C. P. Leticia M. Pérez Gómez
Internal Audit Director



C. P. Sergio Navarrete Reyes
Accounting and Budget Director

See accompanying notes to consolidated financial statements.

**Nacional Financiera, S. N. C.,
Institución de Banca de Desarrollo
and Subsidiaries
Av. Insurgentes Sur 1971, Col. Guadalupe Inn, C.P. 01020, Mexico City**

Consolidated Statement of Income

Year ended December 31, 2017
(With comparative figures for the year ended December 31, 2016, note 4)

(Millions of Mexican pesos)

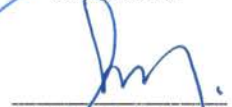
	<u>2017</u>	<u>2016</u> <u>(note 4)</u>
Interest income (note 24)	\$ 33,474	21,191
Interest expense (note 24)	<u>(28,209)</u>	<u>(16,450)</u>
Financial margin	5,265	4,741
Allowance for loan losses	<u>(2,638)</u>	<u>(1,532)</u>
Financial margin adjusted for allowance loan losses	2,627	3,209
Commission and fee income (note 24)	2,825	2,771
Commission and fee expense (note 24)	(231)	(289)
Financial intermediation income (note 24)	(1,208)	(746)
Other operating income (expenses)	1,093	137
Administrative and promotion expenses	<u>(3,261)</u>	<u>(3,179)</u>
Operating income	1,845	1,903
Equity method in the results of unconsolidated subsidiaries and affiliates	<u>6</u>	<u>(6)</u>
Income, before income taxes	1,851	1,897
Current income taxes (note 21)	(777)	(794)
Deferred income taxes (note 21)	<u>433</u>	<u>279</u>
Net income	1,507	1,382
Non-controlling interest	<u>(5)</u>	<u>(29)</u>
Net income	<u>\$ 1,502</u>	<u>1,353</u>


These consolidated statements of income were prepared in accordance with the Accounting Criteria for credit institutions issued by National Banking and Securities Commission, based on Articles 99, 101, and 102 of the Law for Credit Institutions which are of a general and mandatory nature and have been applied on a consistent basis. Accordingly they reflect the transactions carried out by the Institution for the years noted above. Furthermore, these transactions were carried out and valued in accordance with sound banking practices and the applicable legal and administrative provisions.


These consolidated statements of income could be searchable on the following webpage http://www.nafin.com/portafolio/content/nafin-en-cifras/informacion-financiera/estados_financieros.html and <http://portafolioinfo.cnbv.gob.mx/Paginas/contenidos.aspx?ID=37&Titulo=Banca%20de%20Desarrollo>

These consolidated statements of income were approved by the Board of Directors, under the responsibility of the following officers.


Dr. Jacques Rogozinski Schtulman
General Director


C. P. Letizia M. Pérez Gómez
Internal Audit Director


Dr. Federico Ballí González
Deputy General Director of Finance and
Administration


C. P. Sergio Navarrete Reyes
Accounting and Budget Director

See accompanying notes to consolidated financial statements.

Nacional Financiera, S.N.C.
 Institución de Banca de Desarrollo
 and Subsidiaries
 Av. Insurgentes Sur 1971, Col. Guadalupe Inn, C.P. 01020, Mexico City

Consolidated Statements of Changes in Stockholders' Equity
 Year ended December 31, 2017
 (With comparative figures for the year ended December 31, 2016, note 4)
 (Millions of Mexican pesos)

	Paid in capital					Earned Capital					Total Stockholders' equity
	Capital Stock	Contributions for future capital stock increases formalized by the Board of Directors	Paid Stock Premium	Statutory Reserves	Retained earnings	Result from valuations of available-for-sale securities	Effects of valuation in associate and affiliate companies	Remeasurements of defined employee benefits	Net Income	Non-controlling interest	
Restated balances as of December 31, 2015	\$ 8,805	1,550	8,922	1,730	1,436	(290)	289	-	1,284	1,260	25,386
Changes resulting from stockholders' resolutions	-	-	-	-	1,284	-	-	-	(1,284)	-	800
Appropriation of prior year income	-	800	-	-	-	-	-	-	-	-	-
Contributions for future capital stock increases	-	-	-	-	-	-	-	-	-	-	800
Total	-	800	-	-	1,284	-	-	-	(1,284)	-	800
Changes related to the recognition of comprehensive income	-	-	-	-	-	-	-	-	-	-	-
Net income	-	-	-	-	-	-	-	-	1,350	-	1,350
Result from valuation in associated and affiliated companies	-	-	-	-	-	-	351	-	-	-	351
Result from valuation of available-for-sale securities	-	-	-	-	-	112	-	-	-	-	112
Non-controlling interest	-	-	-	-	-	-	-	-	(29)	139	110
Total comprehensive income	-	-	-	-	-	112	351	-	1,321	139	1,923
Balances as of December 31, 2016, previously reported	8,805	2,750	8,922	1,730	2,720	(178)	640	-	1,321	1,399	28,109
Restatement effects (note 4)	-	-	-	-	75	-	-	(574)	32	-	(467)
Restated balances as of December 31, 2016	8,805	2,750	8,922	1,730	2,795	(178)	640	(574)	1,353	1,399	27,642
Changes resulting from stockholders' resolutions	-	-	-	-	1,353	-	-	-	(1,353)	-	-
Appropriation of prior year income	-	2,950	-	-	-	-	-	-	-	-	2,950
Contributions for future capital stock increases (note 22)	-	-	-	-	-	-	-	-	-	-	-
Total	-	2,950	-	-	1,353	-	-	-	(1,353)	-	2,950
Changes related to the recognition of comprehensive income	-	-	-	-	-	-	-	-	-	-	-
Net income	-	-	-	-	-	-	-	-	1,507	-	1,507
Result from valuation in associated and affiliated companies (note 22)	-	-	-	-	-	-	102	-	-	-	102
Result from valuation of available-for-sale securities (note 22)	-	-	-	-	-	286	-	-	-	-	286
Remeasurements of defined employee benefits (note 22)	-	-	-	-	-	-	-	361	-	-	361
Non-controlling interest	-	-	-	-	-	-	-	-	(5)	19	14
Total comprehensive income	-	-	-	-	-	286	102	361	1,502	19	2,270
Balances as of December 31, 2017	\$ 8,805	5,700	8,922	1,730	4,148	108	742	(213)	1,502	1,418	32,862

These consolidated statements of changes in stockholders' equity were prepared in accordance with the Accounting Criteria for credit institutions issued by National Banking and Securities Commission, based on Articles 99, 101, and 102 of the Law for Credit Institutions which are of a general and mandatory nature and have been applied on a consistent basis. Accordingly they reflect the transactions carried out by the Institution for the years stated above. Furthermore, these transactions were carried out and valued in accordance with sound banking practices and the applicable legal and administrative provisions.

These consolidated statements of changes in stockholders' equity could be searchable on the following webpage: http://www.nafin.com/portafin/content/nafin-en-claras/informacion-financiera/estados_financieros.html and <http://portalofinfor.cnbv.gob.mx/Paginas/contenidos.aspx?ID=37&Titulo=Banca%20de%20Desarrollo>

These consolidated statements of changes in stockholders' equity were approved by the Board of Directors, under the responsibility of the following officers.

J. Jacques Rogozinski Semalua
 General Director

Dr. Ricardo Balli González
 Deputy General Director of Finance and Administration

C. P. Leyla M. Pérez-Gómez
 Internal Audit Director

C. P. Sergio Navarro Reyes
 Accounting and Budget Director

See accompanying notes to consolidated financial statements.

Nacional Financiera, S. N. C.,
Institución de Banca de Desarrollo
and Subsidiaries
Av. Insurgentes Sur 1971, Col. Guadalupe Inn, C.P. 01020, Mexico City

Consolidated Statement of Cash Flows

Year ended December 31, 2017

(With comparative figures for the year ended December 31, 2016, note 4)

(Millions of Mexican pesos)

	<u>2017</u>	<u>2016</u> <u>(note 4)</u>
Net Income	\$ 1,502	1,353
Adjustments for items not requiring cash flow:		
Allowance for uncollectible or doubtful accounts	195	161
Depreciation of premises, furniture and equipment	35	38
Provisions	(181)	(131)
Current and deferred income taxes	344	515
Equity method of unconsolidated subsidiaries and affiliates	(6)	6
Others, mainly valuation at fair value	(523)	(579)
	<u>(136)</u>	<u>10</u>
Operating activities:		
Change in margin accounts	(34)	20
Change in investment securities	24,610	(58,755)
Change in debtors on repurchase/ resell agreements	(2,698)	293
Change in derivatives (asset)	(6,755)	7,842
Change in loan portfolio (net)	(14,845)	(34,079)
Change in foreclosed assets	-	5
Change in other operating assets	8,647	(20,777)
Change in deposit funding	9,650	28,759
Change in bank and other borrowings	(4,368)	3,793
Change in creditors on repurchase/ resell agreements	(13,923)	66,596
Change in derivatives (liability)	9,981	(2,233)
Change in other operating liabilities	(102)	550
Payments of income taxes	(393)	(953)
Net cash flows from operating activities	<u>9,770</u>	<u>(8,939)</u>
Investing activities:		
Proceeds from sale of property, furniture and equipment	-	13
Payments for acquisition of property, furniture and equipment	(19)	(1)
Proceeds from disposal of subsidiaries and associates	136	114
Payments for acquisition of subsidiaries and associates	(116)	(1,337)
Collections of cash dividends	4	4
Net cash from (used in) investing activities	<u>5</u>	<u>(1,207)</u>
Financing activities:		
Contributions for future capital stock increases	<u>2,950</u>	<u>800</u>
Net cash flow from financing activities	<u>2,950</u>	<u>800</u>
Net increase (decrease) in cash and cash equivalents	14,091	(7,983)
Effects from cash and cash equivalents value changes	(1,238)	3,161
Cash and cash equivalents at beginning of year	<u>15,698</u>	<u>20,520</u>
Cash and cash equivalents at end of year	<u>\$ 28,551</u>	<u>15,698</u>

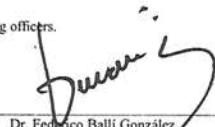
These consolidated statement of cash flows were prepared in accordance with the Accounting Criteria for credit institutions issued by National Banking and Securities Commission, based on Articles 99, 101, and 102 of the Law for Credit Institutions which are of a general and mandatory nature and have been applied on a consistent basis. Accordingly they reflect the transactions carried out by the Institution for the years noted above. Furthermore, these transactions were carried out and valued in accordance with sound banking practices and the applicable legal and administrative provisions.

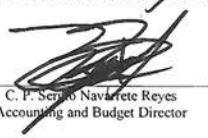
These consolidated statement of cash flows could be searchable on the following webpage http://www.nafin.com/portafolio/content/nafin-en-cifras/informacion-financiera/estados_financieros.html and <http://portafolioinfo.cnbv.gob.mx/Paginas/contenidos.aspx?ID=37&Titulo=Banca%20de%20Desarrollo>

These consolidated statement of cash flows were approved by the Board of Directors, under the responsibility of the following officers.


 Dr. Jacques Rogozinski Sztulman
 General Director


 C. P. Letisia M. Pérez Gómez
 Internal Audit Director


 Dr. Federico Ballí González
 Deputy General Director of Finance and Administration


 C. P. Sergio Navarrete Reyes
 Accounting and Budget Director

See accompanying notes to consolidated financial statements.

**Nacional Financiera, S. N. C.,
Institución de Banca de Desarrollo
and Subsidiaries**

Notes to the Consolidated Financial Statements

For the year ended December 31, 2017
(With comparative figures at December 31, 2016)

(Millions of Mexican pesos)

(1) Description of business -

Nacional Financiera, S. N. C. Institución de Banca de Desarrollo (the Institution), was incorporated on June 30, 1934, by Federal Government Decree as an instrument of significant social and economic transformations, with the purpose of promoting the securities market and foster the mobilization of the financial resources of Mexico.

The Institution operates as a development banking institution, in accordance with its internal regulations, the Credit Institutions Law and the General Provisions Applicable to Credit Institutions (the Provisions) issued by the National Banking and Securities Commission (the Banking Commission).

The Institution's purpose is to contribute to the development of entities, by providing access to financing, training, technical assistance and information, in order to foster their competitiveness and the productive investment; promote the development of strategic and sustainable projects for the country, in an orderly and focused manner, under schemes that allow correction of market failures in coordination with other development banks; promote the regional and sectoral development of the country, particularly in the states with less development, through a differentiated product offer and according to the productive vocations of each region: developing the financial markets and the venture capital industry in the country, to serve as sources of financing for entrepreneurs and small and medium enterprises; to be an Institution with an effective management, based on a consolidated structure of corporate government, that ensures a continuous and transparent operation, as well as the preservation of its capital and to not represent a financial burden for the Federal Government.

In accordance with the provisions of article 2nd. of the internal regulation, the Institution has the goal of promoting savings and investment, as well as channeling financial and technical support to industrial development and, in general, to the national and regional economic development of the country.

(Continued)

**Nacional Financiera, S. N. C.,
Institución de Banca de Desarrollo
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Notes to the Consolidated Financial Statements

(Millions Mexican of pesos)

The Institution operates according to the applicable legal framework and sound banking practices and applications to achieve the general objectives outlined in the article 4th of the Credit Institutions Law, which establishes that the state shall exercise the rectory of the mexican banking system, thus the Institution basically directs its activities to support and promote the development of the country's productive system and the growth of the national economy, based on an economic sovereign policy, by promoting savings in all sectors and regions of Mexico and its appropriate channeling to an extensive regional coverage that is conducive to the decentralization of the mexican banking system, with adherence to sound practices and banking applications.

Development banking institutions are oriented to the productive activities determined by the Union Congress as a specialty of each one of these, in the respective internal regulations.

The Institution carries out its operations according to financing criteria for development banking, channeling their resources mainly through the first tier banking and non-banking financial intermediaries. The main funding sources for the Institution arise from loans from international development institutions such as the International Bank for Reconstruction and Development and the Inter-American Bank of development (IADB), lines of credit from foreign banks and placement of securities in the national and international financial markets.

At December 31, 2017 and 2016, the Institution and its consolidated subsidiaries are integrated as follows:

- i. Operadora de Fondos Nafinsa, S. A. de C. V.* - Which aims to contribute to the development of financial markets, promoting access to the securities market to small and medium investors.
- ii. Corporación Mexicana de Inversiones de Capital, S. A. de C. V.* - Incorporated on February 2, 2006, being its main activity, buy, sell and invest in companies, institutions and private equity funds, as well as promote productive investment in Mexico in the medium and long term, promoting the institutionalization, development and competitiveness of the small and medium enterprises.

(Continued)

**Nacional Financiera, S. N. C.,
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Notes to the Consolidated Financial Statements

(Millions of Mexican pesos)

- iii. *Fideicomiso programa de venta de títulos en directo al público* – Manages the trust funds and carries out the necessary actions to develop and implement the Program for the sale of securities directly to the public, in accordance with the operation rules, which, in the event, the Technical Committee of the Trust authorizes.
- iv. *Fideicomiso 11480 fondo para la participación de riesgos* - Its purpose is having entities which allow to fulfill compliance with the institutional objectives related to the access of micro, small and medium-sized companies in the country to formal finance. The Institution implemented the guarantee program, in order to share with financial banking and non-banking institutions, (intermediaries) determined by the Technical Committee of the trust, the credit risk of the financing granted to companies and national individuals.
- v. *Fideicomiso 11490 fondo para la participación de riesgos en fianzas* – Its purpose is sharing with the country's bonding institutions, established in accordance with the Federal law for institutions of bonds determined by the Technical Committee of the trust, the risk of default on administrative bonds and/or supply concerning the section III, article 5 of the law of bonds, granted to micro, small and medium-sized enterprises, as well as to individuals with entrepreneurial activity, which have signed a contract of supply of goods, services and public works with the Federal public administration.
- vi. *Plaza Insurgentes Sur, S. A. de C. V.* - Its purpose is providing to the Institution, integral real estate services through the leasing of space and furniture, as well as adaptation of offices with preventive and corrective maintenance programs to real estate infrastructure.
- vii. *Pissa Servicios Corporativos, S. A. de C. V. (in liquidation)*- Provides complementary or auxiliary services in the administration or in the realization of the corporate purpose of any national credit entity that is or becomes its shareholder, as well as auxiliary companies and trusts thereof.

At December 31, 2017 and 2016, the operations structure of the Institution abroad, includes two branches located in London, England and another in the Grand Cayman Islands.

(Continued)

**Nacional Financiera, S. N. C.,
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Notes to the Consolidated Financial Statements

(Millions of Mexican pesos)

(2) Financial statement authorization and presentation -

Authorization

On February 16, 2018, Dr. Jacques Rogozinski Schtulman (General Director), Dr. Federico Ballí González (Deputy General Director of Finance and Administration), C. P. Leticia Pérez Gómez (Internal Audit Director) and C. P. Sergio Navarrete Reyes (Accounting and Budget Director) authorized the issuance of the consolidated financial statements and related notes.

The Institution's Board of Directors and the Banking Commission are empowered to modify the consolidated financial statements after issuance. The 2017 consolidated financial statements have been approved at the meeting of the Board of Directors.

Basis of presentation

a) Statement of compliance

The accompanying consolidated financial statements have been prepared, based on the banking legislation, in conformity with the accounting criteria established by the Banking Commission for credit institutions in Mexico. The Banking Commission is responsible for the inspection and supervision of financial institutions, as well as reviewing their financial information.

The accounting criteria provide that in the absence of an specific accounting criterion of the Banking Commission for credit institutions, and in a wider context the Mexican Financial Reporting Standards (MFRS), issued by the Mexican Board of Financial Reporting Standards (Consejo Mexicano de Normas de Información Financiera, A. C. or CINIF), the suppletory process as established by MFRS A-8 shall be applicable, and only when the International Financial Reporting Standards (IFRS) referred to by MFRS A-8 do not resolve the accounting treatment, the suppletory application of an accounting standard pertaining to other regulatory framework may be opted for, providing all the requirements set out by the MFRS are met by the standard. The suppletory application shall be in the following order: U.S. Generally Accepted Accounting Principles (US GAAP), and later any other formal and recognized accounting standard, provided they do not contravene the accounting criteria of the Banking Commission.

(Continued)

**Nacional Financiera, S. N. C.,
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Notes to the Consolidated Financial Statements

(Millions of Mexican pesos)

b) Use of estimates and judgments

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period. The significant financial statement captions subject to such estimates and assumptions include the valuation of financial instruments estimated useful lives for furniture and equipment, allowance for loan losses, employees' benefits and the future realization and deferred taxes. The actual results may differ from those estimates and assumptions.

c) Functional and reporting currency

The aforementioned consolidated financial statements are presented in Mexican pesos, which is the same as the recording currency and the functional currency.

For purposes of disclosure in the notes to the consolidated financial statements, "pesos" or "\$" refers to millions of Mexican Pesos, and when reference is made to "dollars" or "USD", it means millions of dollars of the United States of America.

d) Recognition of assets and liabilities for financial instruments

Assets and liabilities related to the purchase and sale of foreign currencies, investment in securities, securities repurchase/resell agreements and derivatives are recognized in the consolidated financial statements on the trade date, regardless of the settlement date.

(3) Summary of significant accounting policies

The accounting policies shown in this note have been applied on a consistent basis in the preparation of the consolidated financial statements.

(Continued)

**Nacional Financiera, S. N. C.,
Institución de Banca de Desarrollo
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Notes to the Consolidated Financial Statements

(Millions of Mexican pesos)

a) Recognition of the effects of inflation-

The accompanying consolidated financial statements include the recognition of inflation based on Investment Units (Unidades de Inversión or UDI) until December 31, 2007, according to the applicable accounting criteria.

The years ended December 31, 2017 and 2016 are considered non-inflationary economic environment (inflation accumulated over the three preceding years less than 26%), as established in MFRS B-10 "Effects of Inflation", consequently the effects of inflation on the Institution's financial information are not recognized. Should be back in an inflationary environment, the cumulative effects of inflation not recognized in prior periods must be retrospectively recognized from the last period that the economic environment was considered as inflationary. The accumulated inflation rate of the three preceding years is shown as follows:

<u>December 31</u>	<u>UDI</u>	<u>Inflation</u>	
		<u>Annual</u>	<u>Accumulated</u>
2017	\$ 5.934551	6.68%	12.60%
2016	5.562883	3.38%	9.97%
2015	5.381175	2.10%	10.39%
	=====	=====	=====

(b) Cash and cash equivalents-

Cash and cash equivalents consist of cash in hand, deposits with banks in pesos and dollars, as well as 24, 48 and 72 hours foreign currency purchase and sale transactions. Also includes restricted cash and cash equivalents comprised of bank borrowings with original maturities of up to three days ("Call Money"), and deposits in Banco de México (Central Bank) which include the regulation monetary deposits that the Institution is required to maintain in conformity with the provisions issued by the Central Bank for the purpose of regulating liquidity in the financial market; the deposits lack term and bear interest at the average funding rate, in income statement as accrued.

(Continued)

**Nacional Financiera, S. N. C.,
Institución de Banca de Desarrollo
and Subsidiaries**

Notes to the Consolidated Financial Statements

(Millions of Mexican pesos)

The cash and cash equivalents are recognized at nominal value. For the currencies in dollars, the exchange rate used for the translation is the one published by the Central Bank. The translation effect is recognized in the results, as interest income or interest expense, accordingly.

Immediate collection notes will be recorded as other cash equivalent according to what is mentioned as follows:

- Transactions with Mexican entities: two business days after the transaction took place.
- Transactions with foreign entities: five business days after the transaction took place.

When the notes mentioned in the above mentioned paragraph are not collected within the established deadlines, the related amounts will be transferred to the originating item, as applicable, either “Other accounts receivable” or “Loan portfolio”, and due consideration should be given to the provisions of criterion A-2, “Application of particular standards”, and B-6 “Loan portfolio”, respectively.

Transactions transferred to sundry debtors under the caption “Other accounts receivable”, not settled within fifteen days following the transfer date will be classified as past-due debts and an allowance for their total amount recorded will be recorded concurrently.

Notes received subject to collection are recorded in memorandum accounts under the caption “Other accounts”.

(Continued)

**Nacional Financiera, S. N. C.,
Institución de Banca de Desarrollo
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Notes to the Consolidated Financial Statements

(Millions of Mexican pesos)

Checking account overdrafts, as reported in the statement of account issued by the corresponding credit institution, are shown in the caption “Sundry creditors and other accounts payable”.

Likewise, the offset balance of receivable currencies against deliverable currencies, in case this offset results negative.

The foreign exchange currencies acquired and agreed to be settled in purchase transactions to 24, 48 and 72 hours, are recognized as restricted cash (foreign currency for received), while the currency sold is recorded as cash outflow (foreign currency for delivery). The rights and obligations for the sales and purchases of foreign exchange at 24, 48 and 72 hours are recorded in clearing accounts under the caption "Other accounts receivable, net" and "Creditors on settlement of transactions", respectively.

(c) *Margin accounts-*

The margin accounts granted in cash required to the Institution to operate derivatives in recognized markets are recorded at par value and presented in the caption “Margin accounts”. The value of margin accounts granted in cash is modified by margin calls or withdrawals made by the clearing house and for additional contributions or withdrawals made by the Institution.

Returns and commissions affecting the margin accounts, other than fluctuations in derivatives prices, are recognized in result of operations for the year as accrued under “Interest income” and “Commission and fee expense”, respectively. The partial or total amounts deposited or withdrawn in the clearinghouse owing to price fluctuations of derivatives are recognized in “Margin accounts”.

(Continued)

**Nacional Financiera, S. N. C.,
Institución de Banca de Desarrollo
and Subsidiaries**

Notes to the Consolidated Financial Statements

(Millions of Mexican pesos)

(d) Investment securities-

Investment securities consist of equities, government securities, bank promissory notes, and other debt securities listed in recognized markets, which are classified using the categories shown below, based on the intention and capability of management of the Institution on their ownership.

Trading securities-

Trading securities are those acquired with the intention of selling to get short-term gains arising from differences in prices resulting from its trading in the market. Securities at the time of acquisition are accounted for at fair value (which includes, where applicable, the discount or premium) which presumably corresponds to the price paid; transaction costs for the acquisition of securities are recognized in income on the same date.

Subsequently, securities are valued at fair value provided by an independent price vendor; when the securities are sold, the result of buy/sell is determined by the difference between purchase price and the sale price; this shall cancel the result of valuation that has been previously recognized in the income statement.

Interest earned from debt securities are determined according to the effective interest method and are recognized in the year's income under the caption "Interest income".

Dividends from equity securities are recognized in the year's income when the right to receive payment arises under the caption "Interest income".

Valuation effects and purchase or sale results are recognized in the year's income within the caption "Financial intermediation income".

(Continued)

**Nacional Financiera, S. N. C.,
Institución de Banca de Desarrollo
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Notes to the Consolidated Financial Statements

(Millions of Mexican pesos)

Available for sale securities-

Available-for-sale securities are those whose intention are not oriented to profit from differences in prices in the short term or does not have the intention or capacity to hold to maturity. The initial recognition and subsequent valuation is performed in the same manner as trading securities, except that the effect of valuation is recognized in stockholders' equity under the caption "Result from valuation of available-for-sale securities", and which is adjusted by the effect of deferred taxes, which is cancelled for its recognition in income at the time of sale within the caption of "Financial intermediation income". Accrued interest is recognized under the effective interest method under "Interest income or expense".

Interest earned is determined according to the effective interest method and are recognized in the year's income under the caption "Interest income".

Dividends from equity instruments are recognized in the year's income when the right to receive payment arises in the financial statements caption "Interest income".

Held to maturity securities -

Are those debt securities with fixed or determinable payments and with fixed maturity, regarding which the entity has the intention and capacity to hold until maturity. These securities are initially recognized at fair value which is presumably the price paid; and later are valued at amortized cost, which implies that the amortization of the premium or discount as well as the transaction costs form part of interest earned recognized in income under "Interest income". Interest is recognized in income as earned and when the securities are sold, the sales gain or loss is recognized for the difference between the net realizable value and the book value of the securities within the caption of "Financial intermediation income".

(Continued)

**Nacional Financiera, S. N. C.,
Institución de Banca de Desarrollo
and Subsidiaries**

Notes to the Consolidated Financial Statements

(Millions of Mexican pesos)

Security's impairment-

Where sufficient objective evidence exists that a security available-for-sale or held-to-maturity has been impaired because of one or more events that occurred after initial recognition of security, the carrying amount of the security is modified and the impairment is recognized in the year-end results under the caption "Financial intermediation income". Regarding available-for-sale securities, the amount of loss recognized in equity is canceled.

If, in a subsequent period, the fair value of the security increases, and this effect is related objectively to an event occurring after the impairment was recognized in the income statement, the impairment is reversed in the year's results, except if it is an equity instrument.

Value date transactions-

Securities acquired where settlement takes place on a subsequent date, up to a maximum of four business days following the date of the purchase-sale transaction, are recognized as restricted securities, while securities sold are recognized as securities to be delivered, and are deducted from investments securities; the counter entry is a credit or debit to a settlement account, as applicable. Where the amount of securities to be delivered exceeds the balance of own securities of the same type in position (government, bank, equity and other debt securities), this is reflected as a liability under "Traded securities to be settled".

Reclassification between categories-

The accounting criteria allows reclassifications from held-to-maturity to available-for-sale securities, provided it is not intended to hold them until maturity. Valuation adjustments at the date of the reclassifications are recognized in stockholders' equity. In the case of reclassifications of securities to the category held to maturity, or of securities from trading to available for sale, this is only permissible with the express authorization of the Banking Commission.

(Continued)

Nacional Financiera, S. N. C.,
Institución de Banca de Desarrollo
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Notes to the Consolidated Financial Statements

(Millions of Mexican pesos)

(e) Repurchase/resell agreements -

At the trade date of the repurchase/resell agreement transaction (repo), the Institution acting as seller recognizes either the cash inflow or a debit clearing account, as well as an account payable, whereas when acting as buyer recognizes either the cash outflow or a credit clearing account, as well as an account receivable. Both the account payable and the account receivable are initially stated at the agreed-upon price, representing the obligation to repay or the right to recover the cash, respectively.

Over the term of the repo, the account receivable and the account payable are valued at the amortized cost, recognizing the interest on repos in the result of operations for the year as earned, in accordance with the effective interest method. The interest is recognized under the financial statement caption "Interest income" or "Interest expense", as appropriate. The account receivable and the account payable, as well as the interest earned are reported in the financial statement caption "Debtors on repurchase/resell agreements" and "Creditors on repurchase/resell agreements", respectively.

The Institution acting as repurchase recognizes the received collateral in memorandum accounts within the caption of "Collateral received by the entity", in accordance with accounting criterion B-9 "Assets in custody and under management". Financial assets granted as collateral, when the Institution acting as repurchaser, the financial asset is reclassified on the consolidated balance sheet within the caption of "Investment securities", reporting it as a restricted asset.

Should the Institution, acting as repurchase sell or pledge the collateral, the transaction proceeds and an account payable is recorded for the obligation to return the collateral to the repurchaser, which is valued, in the case of sale at fair value, or if pledged in another sale and repurchaser agreement, at amortized cost. The account payable is offset with the account receivable, which is recognized when the Institution acting as repurchase turn becomes as repurchaser and the debit or credit balance is presented in the consolidated financial statement caption "Debtors on repurchase/resell agreements" or in "Collateral sold or pledged", as applicable.

(Continued)

Nacional Financiera, S. N. C.,
Institución de Banca de Desarrollo
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Notes to the Consolidated Financial Statements

(Millions of Mexican pesos)

Additionally, the collateral received, delivered or sold is recognized in memorandum accounts within the caption of "Collateral received and sold or pledged by the entity", in accordance with accounting criterion B-9 "Assets in custody and under management".

(f) Derivatives-

Transactions with derivative financial instruments comprise those carried out for trading and hedging purposes. Irrespective of their purpose, the derivatives are recognized at fair value.

The valuation effect of the derivatives for trading purposes is shown in the consolidated balance sheet and consolidated statement of income under "Derivatives", in the assets or liabilities, accordingly, and "Financial intermediation income", respectively. The effect of the derivatives credit risk (counterparty), must be determined according to the risk area methodology, and must be recognized in results in the period in which it occurs against the supplementary account.

The effective portion of the valuation adjustments of hedges designated for cash flow purposes is recognized in stockholders' equity, under the caption "Unrealized result from valuation of cash flow hedge instruments", while the ineffective portion of the change in fair value is recognized immediately in the consolidated income statement under "Financial intermediation income", and the counter-account with such effect are presented in the consolidated balance sheet under "Derivatives". The gain or loss associated with the coverage of the forecasted transaction that has been recognized in stockholders' equity, is reclassified to the consolidated statement of income within the same caption that presents the result of valuation of hedged party attributable to the hedged risk, in the same period during which the hedged forecasted cash flows affect the year's results of operations.

(Continued)

Nacional Financiera, S. N. C.,
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Notes to the Consolidated Financial Statements

(Millions of Mexican pesos)

If the cash flow hedge derivative reaches maturity, is exercised, terminated or the hedge does not meet the requirements to be deemed effective, the hedge designation is de-designated, while the valuation of the cash flow hedge derivative within stockholders' equity remains in this caption and is recognized in the year's results when the forecast transaction occurs, in the same caption which presents the gain or loss of the valuation attributable to the hedged risk.

The gain or loss arising from valuing the fair value hedge derivative is recognized in the consolidated balance sheet under "Derivatives" and in the consolidated statement of income in "Interest income" and "Financial intermediation income", since they correspond to interest rate hedges of loan portfolio and investments securities classified as available-for-sale, respectively. The result of valuation of the item attributable to the hedged risk is recognized on the consolidated balance sheet under "Valuation adjustments from hedging of financial assets" and recognized in the year's income in the case of loan portfolio, in "Interest income", while for investments securities classified as available-for-sale, in "Financial intermediation income".

Collaterals pledged and received in derivate transactions carried out over-the-counter -

The collateral is a security obtained to ensure payment of the price agreed in contracts with derivative financial instruments on over-the-counter transactions.

The granting of collateral pledged in cash in derivative over-the-counter transactions are recorded as account receivable under the caption "Other accounts receivables", while collateral received in cash are recorded as "Other accounts payable".

The collaterals pledged in securities are recorded as restricted securities by guarantees, and the collaterals received in securities from derivatives transactions are recorded in memorandum accounts.

(Continued)

**Nacional Financiera, S. N. C.,
Institución de Banca de Desarrollo
and Subsidiaries**

Notes to the Consolidated Financial Statements

(Millions of Mexican pesos)

(g) Settlement clearing accounts-

Amounts receivable or payable for investment securities, securities repurchase/resell agreements, and/or derivatives, which have expired but have not been settled at the consolidated balance sheet date, including the amounts receivable or payable for purchase or sale of foreign currencies, which are not for immediate settlement or those with a same day value date, are recorded in clearing accounts.

The balances of clearing accounts, credit and debit are offset as long as it has the contractual right to offset amounts recognized, there is an intention to settle on a net basis, realize the asset and settle the liability simultaneously.

The clearing accounts are shown under the financial statement caption “Other accounts receivable, net” or “Creditors on settlement of transactions”, as appropriate.

(h) Loan portfolio-

Represents the balance of the total or partial dispositions of credit lines granted to the borrowers plus uncollected accrued interest, less the interest collected in advance. The allowance for credit risks is presented by deducting the balances of the credit portfolio.

Undrawn credit facilities are recorded in suspense accounts, under “Loan commitments”. The withdrawn amount is recorded into the loan portfolio in the caption of the portfolio as appropriate.

At the time of contracting, transactions with letters of credit are recorded in memorandum accounts under “Loan commitments” which, upon being used by the client or its counterparty are transferred to the loan portfolio.

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Past-due loans and interest -

Outstanding loans and interest balances are classified as past due according to the following criteria:

1. Knowledge that the borrower has filed for bankruptcy, under the Bankruptcy Law.

An exemption exist from the rule mentioned in the paragraph above mentioned, for those loans that continues receiving payment in terms of the Bankruptcy Law under section VIII of article 43, as well as those loans granted under article 75, in relation to sections II and III of article 224 of the mentioned Law, however, if incurred in one of the cases provided in the following numeral 2, they will be recorded as past-Due loan portfolio.

2. Its installments have not been fully settled on the terms originally agreed, considering the following:
 - a) If the debts consist in loans with a single payment of principal and interest at maturity, and have 30 or more calendar past-due days;
 - b) If the debts refer to loans with a single payment of principal at maturity and periodic payments of interest, and the related interest payment has 90 or more calendar past-due days, or principal has 30 or more calendar past-due days;
 - c) If debts consist of loans with principal and interest periodic partial payments, including mortgage loans, have 90 or more calendar past-due days;

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- d) If debts consist of revolving loans, and unpaid for two monthly normal billing periods or, where the billing period is other than monthly, when have 60 or more calendar past-due days; and
- e) Overdrafts from checking accounts, and immediate payment notes receivable, upon occurrence of such event.

When a loan is transferred to the past-due portfolio, accrual of interest is discontinued and record thereof is kept in memorandum accounts. Also suspending the amortization in financial income accrued in the year's results. Once collected, such interest is recognized directly in consolidated income statement under "Interest income". Recognition in consolidated income statement of interest income resumes when the portfolio ceases to be considered as past due.

An allowance is constituted for an amount equal to the total of uncollected accrued interest corresponding to loans deemed past-due at the time the loan is transferred to the past-due portfolio. For past-due loans, which restructuring agrees to the capitalization of earned, uncollected interest previously recorded in memorandum accounts, an allowance is created for the total of such interest amount. The allowance is released when there is evidence of sustained payment.

Past-due loans are reclassified as current when the unpaid balances have been fully paid by the debtor (principal and interest, etc.), except for restructured loans or renewed, which are transferred to current portfolio when sustained payment has been made.

Sustained payment -

It is considered that there is sustained payment when the borrower shows compliance of the payment without delay for the total amount of principal and interest, for at least three consecutive amortizations of the loan payment scheme, or in the case of loans with amortizations that cover periods greater than 60 calendar days, the payment of an exhibition.

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In loans with periodic payments of principal and interest whose amortizations are less than or equal to 60 days in which the periodicity of payment to minor periods is modified due to the application of a restructuring, a sustained payment of the loan is considered, when the borrower shows payment of amortizations equivalent to three consecutive amortizations of the original loan scheme.

In the case of consolidated loans, if two or more loan originate the reclassification to the caption "Past-due loan portfolio", in order to determine the three consecutive amortizations required for the existence of a sustained payment, the original loan repayment scheme should be considered, whose repayments equivalent to the longer term.

Regarding loans with a single payment of principal at maturity, regardless of whether the payment of interest is periodic or at maturity, it is considered that there is a sustained payment of the loan when any of the following assumptions occur:

- a) the borrower has covered at least 20% of the original amount of the loan at the moment of the restructuring or renewal or,
- b) the amount of interest accrued under the restructuring or renewal payment scheme corresponding to a period of 90 days had been covered.

Prepayment of an amortization of restructured or renewed loan (amortization of restructured or renewed loan that have been paid without the occurrence of natural days equivalent to three consecutive amortizations of the loan amortization schedule or in the case of loans with amortization covering longer periods than 60 calendar days, the payment of an exhibition), other than those with a single payment of principal at maturity, regardless of whether the interest is paid periodically or at maturity, is not considered as a sustained payment.

Restructuring and renewals

Unless there is evidence of sustained payments, past-due loans restructured or renewed shall remain within the past-due loan portfolio.

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Loans with single payment of principal at maturity and periodic interest payments, as well as loans with a single payment of principal and interest at maturity being restructured during the term of the loan or renewed at any time will be considered as nonperforming loans as long as there is no evidence of sustained payment.

Current loans that are restructured or renewed, without at least 80% of the original loan term having elapsed, shall be deemed current only when the borrower had:

- i) Paid the total accrued interest, and
- ii) Paid the original principal loan amount at the renewal or restructuring date.

Current loans that are restructured or renewed during the course of the final 20% of the original term of the loan will be considered as current only when the borrower had:

- i) Fully paid the total interest accrued;
- ii) Covered the total original amount which the date of renewal or restructuring should had been paid, and
- iii) Paid 60% of the original loan amount.

Renewed or restructured loans where the borrower fails to meet the above conditions will be deemed past-due from the renewal or restructuring date until there is evidence that sustained payment are being made.

Those loans considered revolving, which have been restructured or renewed, will be considered as current when the borrower had paid off the totality of accrued interest, there are no invoicing periods past due and there is evidence to prove the debtor's repayment capability.

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Loan due and payable principal and interest amounts which, at the restructuring date, have been repaid in full and for which one or several of the following loan conditions have been changed, shall not be deemed restructured.

- i) Guarantees: only when involving the extension or replacement with better quality guarantees.
- ii) Interest rate: when the agreed-upon interest rate is improved.
- iii) Currency: provided the rate corresponding to the new currency be applied.
- iv) Payment date: only if the change does not represent exceeding or modifying the frequency of payments. In no case shall the change in the payment date enable omitting the payment in any given period.

The loan portfolio restructurings or renewals are made in compliance with the General Provisions applicable to credit institutions and the viability of them is analyzed particularly.

The Institution periodically evaluates if a past-due loan should remain in the consolidated balance sheet or be written-off, provided a provision has been created for 100% of the loan amounts. Such write-off is made by cancelling the unpaid loan balance against the allowance for loan losses previously created for each loan. Any recovery derived from loans that were previously written-off is recognized in the year's results.

Write-downs, cancellations, refunds or discounts are recorded against the provision for loan losses. In case the amount of these items exceeds the provision for loan losses balance related to the loan, a charge to provision is recorded up to the amount of the difference

Costs and expenses related to loan origination

The costs and expenses related to loan origination are recorded as a deferred charge, which is amortized to the income statement under the caption "Interest expense" during the average term of the loans, except for origination of revolving loans, which are amortized over a period of 12 months against the expense caption that corresponds according to its nature.

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Policies and procedures for granting, controlling and recovering of loans

- a) Loans, granted or guaranteed by the Institution, are aimed to finance projects for economic and financial viable companies.
- b) The maximum funding limit is determined based on the needs of the investment project and the assessment of the company or project capacity of payment.
- c) Loans grace periods and terms are established depending on the companies' capacity of payment.
- d) Real guarantees are obtained, preferably mortgage securities in an appropriate and sufficient proportion, according to the loan characteristics and, where appropriate, in accordance with the financial broker that grants it.
- e) Regarding loan guarantees granted by the Institution, these are complementary to those which have to offered by the borrowers and do not substitute those guarantees. Accordingly, brokers should negotiate with the borrowers the guarantees for the loan granted.
- f) The borrower must have a proven integrity and creditworthiness.
- g) Credit granting operations, either for Banking Financial Broker (BFB) and Non-Banking Financial Broker (NBFB), is carried out in the head office. The Institution carries out on monthly basis and quarterly basis a reconciliation of balances with the NBFB and BFB, respectively.
- h) Portfolio turnover is carried out through the Institutional Portfolio Recovery and Administration System (SIRAC), managed by the Credit Administration Office.

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- i) No new credit operations are carried out with the creditor company, as long as there are past-due loans with that company.
- j) Out-of-court collection procedures are realized in the portfolio with 30 to 90 days of default.
- k) Once 90 days of default 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 discounted 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) Financial Brokers modality "A", defined as banks or factoring companies and leasing entities that are part of a financial group. These brokers, given the mechanism of payment, which is a charge in its account in Central Bank, are considered at lower risk scale.

A "Credit Risk Limit Assignment Methodology for Operating with Banks in Mexico" 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.

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- b) Modality "B" Financial brokers applies to all the NFBF that do not form part of a financial group. 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 for credit risk is established based on the loan portfolio 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 vintage analysis, 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.

(i) Allowance for loan losses-

Allowance for loan losses represents Institution's management best estimate of probable losses inherent in the loan portfolio as well as guarantees issued and irrevocable loan commitments

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Commercial loans - The allowances for the commercial loans are based on the individual assessment of the credit risk of borrowers and their classification, in accordance with the general regulations applicable to the methodology for rating of the loan portfolio of credit institutions, established by the Banking Commission. Commercial loans shall be subject to credit rating without including those loans with express warranty of Entities of the Federal Public Administration under direct budgetary control, productive State enterprises or those indicated in Section VI of Article 112 of the Provisions, in which the allowance percentage shall be equal to 0.5%.

The Provisions use a methodology which classifies the loan portfolio into different groups: in states and municipalities, investment projects with own source of payment, trustees acting under trusts, financial institutions and corporations and individuals with business activity not included in the aforementioned groups; the last group must be divided into two subgroups: corporations and individuals with business activity with annual net sales or revenues greater than 14 million UDIS and less than 14 million UDIS. For purposes of rating projects with own source of payment, the Provisions establish that the rating is calculated using risk analysis of the investment project according to their stage of construction or operation, and through the extra cost of labor and cash flows of the project. For other groups, expected loss methodology is established for credit risk, considering the probability of default, loss given default and exposure at default.

Loan portfolio granted to corporations and individuals with business activity, with annual net revenues or sales lesser than 14 million UDIS, is credit rated through the application of methodology set forth on Appendix 21 of the Provisions. For the financial institutions loans, the methodology set forth-on Appendix 20 of the Provisions is used, which establishes the concept of probability of default, loss severity and exposure at default is used.

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The estimates carried out at December 31, 2017 and 2016, were determined based on the risk levels and allowance percentage according to the following table:

<u>Grade of risk</u>	<u>Range of allowance percentages</u>	
A1	0.000	0.90%
A2	0.901	1.5%
B1	1.501	2.0%
B2	2.001	2.50%
B3	2.501	5.0%
C1	5.001	10.0%
C2	10.001	15.5%
D	15.501	45.0%
E	Higher than 45.0%	

Mortgage loans-

Allowance for loans losses of mortgage is determined using the corresponding balances the last day of each month. Furthermore, factors such as the following are taken into consideration: (i) amount payable; (ii) payment made; (iii) house value; (iv) outstanding loan balance; (v) days of delinquency; (vi) loan denomination; and (vii) file documentation. The total amount to reserve for each assessed loan is the result of multiplying the probability of default for the loss given default and exposure at default.

The risk grades and percentages of allowance for loan losses at December 31, 2017 and 2016, are as shown in next page.

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<u>Grade of risk</u>	<u>Range of allowance percentage</u>	
A1	0.000	0.50%
A2	0.501	0.75%
B1	0.751	1.00%
B2	1.001	1.50%
B3	1.501	2.00%
C1	2.001	5.00%
C2	5.001	10.00%
D	10.001	40.00%
E	40.001	100.00%

Consumer loans-

The methodology followed for both groups is described in articles 91 and 92 of the Provisions, respectively. The total allowance amount for each loan is the result of multiplying the probability of default by the loss given default and exposure to default.

The risk grades and percentages of provision for loan losses at December 31, 2017 and 2016, are shown as follows:

<u>Grade of risk</u>	<u>Ranges of allowance percentage</u>	
A1	0.00	2.0%
A2	2.01	3.0%
B1	3.01	4.0%
B2	4.01	5.0%
B3	5.01	6.0%
C1	6.01	8.0%
C2	8.01	15.0%
D	15.01	35.0%
E	35.01	100.0%

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Impaired loan portfolio – For consolidated financial statement disclosure purposes, the Institution considers impaired loans to those commercial loans for which determine that there is a considerable probability that they could not be recovered in full, without giving consideration to improvements in risk levels resulting from the secured portion of the loan, as are loans that, although current, result from negotiations in which a forgiveness, reduction or settlement was authorized at the end of the agreed-upon term, and loans payable by individuals classified as undesirable customers.

Additional identified reserves– Are established for those loans, which in management’s opinion, may give cause for concern in the future given the particular situation of the customer, the industry or the economy. Furthermore, it includes estimates for items such as normal interest earned but not collected and other items which realization is considered to result in a loss to the Institution, as well as reserves maintained for guarantees granted.

(j) *Other accounts receivable-*

Loans to officers and employees, collection rights and the accounts receivable related to debts whose maturity is agreed from origin to more than 90 calendar days term are evaluated by the Institution’s management to determine the estimated recoverable amount and, as required, to create the corresponding allowance. The balances of other debit items are recorded into the income statement 90 days after their initial recording, if they correspond identified items and 60 days if the balances are unidentified, regardless of their chance of recovery, except for tax-related (VAT included) balances.

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Overdrafts on checking accounts of costumers which do not have a loan facility for such purposes, shall be classified as past-due debts and the Institution must simultaneously create a reserve for such classification for the total amount of the overdraft at the time when such event occurs.

(k) *Foreclosed assets or assets received in lieu of payment-*

Foreclosed assets are recorded on the date the admission order of the judicial sale by which the foreclosure was decreed, became final and conclusive and is immediately available for execution.

Assets received in lieu of payment are recorded on the date the deed of payment, or that on which the transfer of title to the asset is formally executed.

The accounting recognition of a foreclosed assets considers the value of the tangible asset (at the lower of cost or fair value less strictly necessary costs and expenses incurred for foreclosure), as well as the net value of the asset arising the foreclosure. When the net value of the asset arising the foreclosure exceeds the value of the foreclosed asset, the loss is recognized in consolidated income statement caption "Other operating income". Otherwise, the value of the foreclosed asset is adjusted to the net value of the asset.

The value of the asset originating the foreclosure and the relevant loan loss allowance set up as of that date are derecognized from the consolidated balance sheet.

Foreclosed assets and promised for sale are restricted to their carrying value; collections received on account of the asset are recorded as a liability. On the date of sale, the resulting gain or loss is recognized in the consolidated income statement caption "Other operating income".

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Reductions in the value of foreclosed assets are valued according to the type of asset concerned, recording such valuation in the consolidated income statement caption “Other operating income”. The Institution creates additional provisions that acknowledge signs of impairment from potential value losses over time in foreclosed assets in the year’s results of operations under “Other operating income”, which are determined by multiplying the reserve percentage applicable by the value of the foreclosed assets, based on the provisions of foreclosed assets or assets received in payment methodology of the Banking Commission, as show:

Months elapsed from the date of foreclosure or received in lieu of payment	Reserve percentage	
	Real Estate	Receivables, furniture, and equipment and investment securities
Over 6	0%	0%
More than 6 to 12	0%	10%
More than 12 to 18	10%	20%
More than 18 to 24	10%	45%
More than 24 to 30	15%	60%
More than 30 to 36	25%	100%
More than 36 to 42	30%	100%
More than 42 to 48	35%	100%
More than 48 to 54	40%	100%
More than 54 to 60	50%	100%
<u>More than 60</u>	<u>100%</u>	<u>100%</u>

(l) Premises, furniture and equipment -

Premise, furniture and equipment are recorded at acquisition cost. Those assets acquired before December 31, 2007 were adjusted by using factors based on the UDI value from the date of acquisition through that date, which recognition of the effects of inflation on the financial information was suspended according to the MFRS. The components acquired in foreign currency are recorded at the historical exchange rate, that is, the exchange rates in force on the date the asset was acquired.

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Depreciation is calculated using the straight-line method, based on the estimated useful lives by the Institution's management of the corresponding assets.

Depreciation amount of premises, furniture and equipment is determined by subtracting the residual value and, as applicable, the cumulative impairment losses from the acquisition cost. The Institution periodically evaluates premises, furniture and equipment residual values to determine amounts to be depreciated.

The Institution evaluates periodically the net book values of premises, furniture and equipment, to determine whether there is an indication that these values exceed their recoverable amount. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net revenues expected to be generated by the asset. If the net book value of an asset exceeds its recoverable amount, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds the fair value of the asset.

(m) *Permanent investments -*

The permanent investments where there is no control, joint control or significant influence exists are classified as other investments, which are initially recognized and maintained valued at acquisition cost. Dividends, if any, received from these investments are recognized in consolidated statement of income caption "Other operating income", except if are from prior periods to the acquisition, in which case are decreased from the permanent investment

(n) *Other assets-*

This caption includes mainly prepaid expenses and commissions as well as guarantee deposits, which are recognized as an asset on the trade date considering economic future benefits for the Institution.

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In case of any indication of impairment, the potential impairment loss is determined, and if the net carrying value exceeds the recoverable amount, the asset value is written down and the impairment loss is recognized in the results of operations for the year

(o) *Income taxes and employee statutory profit sharing (ESPS)-*

The income taxes and ESPS payable for the year are determined in conformity with the applicable tax provisions.

Income taxes payable are presented as liability in the consolidated balance sheet; when the tax prepayments exceed the income tax payable, the difference corresponds to an account receivable.

Deferred income taxes and deferred ESPS are accounted for under the asset and liability method. Deferred taxes and ESPS assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and in the case of IT for operating loss carryforwards. Deferred tax and ESPS assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred ESPS and taxes assets and liabilities of a change in tax rates is recognized in results of operations for the period enacted.

The deferred income tax asset is periodically valuated creating, where appropriate, valuation allowance for those temporary differences which might exist an uncertain recovery.

The deferred income tax asset or liability determined from the temporary deductible or taxable differences of the year, are presented in the in the consolidated balance sheet.

Current and deferred ESPS is presented in the caption “Administrative and promotional expenses”, in the consolidated statement of income.

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(p) *Deposit funding-*

This caption comprises time deposits of the money market funding, the placement of debt certificates and bank bonds. Interest is charged to expense on an accruals basis under “Interest expense”. For instruments sold at a value different to their face value, the difference is recognized as a deferred charge or credit and amortized on a straight-line basis over the term of the respective instrument.

(q) *Provisions-*

Based on management’s estimates, the Institution recognizes accruals for present obligations where the transfer of assets or the rendering of services is probable and arises because of past events.

(r) *Bank and other borrowings-*

Bank and other borrowings comprise short and long-term loans from domestic and foreign banks, which are recorded based on the contractual value of the obligation. Interest is recognized on accruals basis under the caption “Interest expense”.

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(s) *Employees' benefits -*

Short-term direct benefits

Short-term direct employee benefits are recognized in income of the period in which the services rendered are accrued. A liability is recognized for the amount expected to be paid if the Institution has a legal or assumed obligation to pay this amount as a result of past services provided and the obligation can be reasonably estimated.

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Long-term direct benefits

The Institution's net obligation in relation to direct long-term benefits (except for deferred ESPS - see note income taxes and employee statutory profit sharing), and which the Institution is expected to pay at least twelve months after the date of the most recent consolidated balance sheet presented, is the amount of future benefits that employees have obtained in exchange for their service in the current and previous periods. This benefit is discounted to its present value.

Termination benefits

A liability is recognized for termination benefits along with a cost or expense when the Institution has no realistic alternative other than to make the corresponding payments or when the offer of these benefits cannot be withdrawn or when the conditions that require the recognition of restructuring costs are met, whichever occurs first. If benefits are not expected to be settled wholly within twelve months after the date of the most recent balance sheet presented, then they are discounted.

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Defined benefit plans

In addition, the Institution has a defined benefit plan in place that covers the pensions for retirement, the seniority premiums and legal compensation to which employees are entitled in accordance with the Federal Labor Law, as well as obligations related to corresponding to plans medical benefits, food coupons and life insurance for retirees.

Irrevocable trusts have been established for all plans to manage the respective plan funds and assets.

The calculation of liabilities for defined benefit plans, held annually by actuaries using the projected unit credit method. When the calculation results in a possible asset to the Institution, recognized asset is limited to the present value of the economic benefits available in the form of future refunds from the plan or reductions in future contributions to it. To calculate the present value of the economic benefits, any minimum funding requirements should be considered.

The labor cost of current service, which represents the periodic cost of employee benefits for having completed one more year of working life based on the benefit plans, is recognized in administrative and promotional expenses. The Institution determines the net interest expense (income) on the net defined benefit liability (asset) for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to then-net defined benefit liability (asset), taking into account any changes in the net defined benefit liability (asset) during the period as a result of estimates of contributions and benefit payments.

Modifications to the plans that affect past service cost are recognized in income immediately in the year the modification occurs, with no possibility of deferral in subsequent years. Furthermore, the effects of events of liquidation or reduction of obligations in the period that significantly reduce future service cost and/or significantly reduce the population eligible for benefits, are recognized in income of the period.

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Remeasurements generated as from January 1, 2016 (before actuarial gains and losses) resulting from differences between the projected and actual actuarial assumptions at the end of the period, are recognized when incurred as part of OCI within stockholder's equity and is subsequently recycled to the results of the period, based on the average remaining working life of the employees.

According to the resolution published on December 31, 2015 by the Banking Commission, modifications to the plans and remeasurements accumulated until December 31, 2015, are gradually recognized from 2021 to the next four years.

(t) Revenue recognition-

Interest on loans granted including the interbank loans fixed to a term less than or equal to three business days, is recorded in income as earned. Interest on past-due loans is recognized in income upon collection.

The interest collected in advance and origination loan fees and credit card annual fees are recorded within "Deferred credits and prepayments", and applied to the year's results of operations in "Interest income" and "Commission and fee income", respectively, as accrued, in the term of the loan or during a year, as applicable.

The commissions from assets in custody or under management are recognized in income as accrued in "Commission and fee income". Fees on trust transactions are recognized in income as accrued in "Commission and fee income". Such revenues are not accrued when fees are 90 or more calendar days past due, and are recorded in memorandum accounts. When accrued revenues are collected, they are reported directly in income for the year.

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Fees for restructured or renewed loans are recorded as deferred credits and amortized against the results of operations for the year in “Interest income” using the straight-line method during the new term of the loan.

Income from commissions collected on transactions in the derivative market are recorded in the consolidated statements of income as the service is provided under the caption “Commission and fee income”.

(u) Foreign currency transactions -

Foreign currency transactions are recognized at the exchange rate prevailing on the date of execution, for consolidated financial statement presentation purposes. In the cases of currencies other than dollars are translated into dollars at the exchange rates as established in the Provisions, and the dollar equivalent, together with dollar balances, are then translated into Mexican pesos using the exchange rate determined by the Central Bank.

Foreign exchange gains and losses are reflected in results of operations for the year. At the year-end close date of the consolidated financial statements, foreign currency monetary assets and liabilities are translated into pesos at the FIX exchange rate published by Central Bank, while foreign exchange gains or losses arising from foreign currency translation are recorded in the results of operations for the originating period.

(v) Memorandum accounts-

Memorandum accounts corresponds mainly to assets in custody or management and trust transactions.

Client’s values held in custody, guarantee or under management, are recorded in the corresponding memorandum accounts in accordance with the accounting criteria established by the Banking Commission, and represent the maximum expected amount at which the Institution is obliged to respond to its clients.

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The amounts of the assets in custody or under management are presented in the caption “Assets in custody or under management”, while the trust transactions are presented in the caption “Assets in trust or under mandate”.

(w) Contingencies-

Liabilities or important losses related to contingencies are recorded when it is probable that a liability has been incurred and the amount thereof can be reasonably estimated. When a reasonable estimation cannot be made, qualitative disclosure is provided in the notes to the consolidated financial statements.

Contingent income, earnings or assets are not recognized until their realization is assured.

(4) Accounting changes and restatement adjustments -

Accounting changes 2017-

The accounting changes recognized by the Institution in 2017 were derived from the adoption of the modifications to Banking Commission’s Provisions related to the change in the methodology for rating of non-revolving consumer loans and mortgage as shown below:

(a) Change in the methodology for rating of non-revolving consumer loans and mortgage-

On January 6, 2017, a resolution was issued in the Official Federal Gazette which enters into force on June 1st, 2017, amending the Provisions to adjust the methodology of allowance for loan losses corresponding to non-revolving consumer loans and mortgage loans, these Provisions incorporate new dimensions of risk at customer level, indebtedness, performance of payments and the specific risk profile of each product; as well as, update and adjust the probability of default, risk's parameters, loss given default and exposure at default. The financial impact in the allowance for loan losses must be recorded in 100% no later than twelve months after the entry into force, according to the publication in the Official Federal Gazette from June 26, 2017.

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The financial effects resulting from the changes in the methodology mentioned in the last paragraph of the previous page, were not material in the Institution's consolidated financial statements.

(b) 2017 MFRS Improvements -

In October 2016, CINIF issued the document referred to as "2017 MFRS Improvements", which contains precise modifications to some current MFRS. MFRS Improvements mentioned below that entered into force for the years beginning after the 1st. January 2017 did not generate important effects in the Institution's consolidated financial statements.

- MFRS B-13 *"Subsequent events as date of the financial statements"*
- MFRS B-6 *"Statement of financial position"*
- MFRS C-11 *"Stockholders equity"*
- MFRS D-3 *"Employees' benefits"*

Accounting changes 2016-

The accounting changes recognized by the Institution in 2016, were derived from the adoption of amendments to the provisions of the Banking Commission, relating to the change in the loan portfolio of consumer rating methodology and the adoption of the MFRS D-3 "Employees' benefits", as shown below:

(c) MFRS D-3 "Employees' benefits"-

Progressive implementation of the adoption of MFRS D-3 "Employee benefits" issued by the Banking Commission

On December 31, 2015, a resolution was issued in the Official Federal Gazette that amends the Provisions in which through the third transitory article, the Banking Commission sets out the terms to recognize changes from the adoption of the new MFRS D-3, which enters into force on January 1, 2016, and defines the term that credit institutions have to recognize in its stockholders' equity the total amount of outstanding balances to be amortized from profits or losses of defined benefit plan, as well as modifications to the plan, not recognized until December 31, 2015.

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The resolution states that the institutions referred to in Article 2, Section II of the Credit Institutions Law, opting for the progressive implementation of the transitory article referred to, should start the recognition of the balances listed in numbering a) and b) of paragraph 81.2 of MFRS D-3, no later the year 2021, recognizing 20% of the balances in that year and an additional 20% in each of the subsequent years, up to 100% within a maximum period of 5 years". The Institution has adopted the MFRS D-3 "Employees' benefits" and informed to the Banking Commission.

(d) 2016-MFRS Improvements

On December 2015, CINIF issued the document referred to as "2016 MFRS Improvements", which contains precise modifications to some current MFRS. MFRS Improvements mentioned below that entered into force for the years beginning after the 1st. January 2016 did not generate important effects in the consolidated financial statements of the Institution.

- **MFRS C-7 "Investments in Associates, joint ventures, and other permanent investments"**- It establishes that investments or contributions in kind should be recognized based on its fair value.
- **MFRS B-7 "Business acquisitions"**- MFRS B-7 clarifies that acquisitions of entities under common control are not part of the scope of this MFRS, regardless of how the amount of the consideration was determined.

Restatement adjustments -

The following restatement adjustments were applied to the consolidated financial statements at and for year ended December 31, 2016, in order to have the appropriate presentation in accordance with the accounting criteria applicable to the Institution for the caption of "Financial instruments available for sale" of investments in equity that holds its subsidiary "Corporación Mexicana de Inversiones de Capital, S. A. de C. V.", which were recognized as permanent investments.

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		<u>Balances previously reported</u>	<u>Restatment adjustments</u>	<u>Restated balances</u>
<u>Balance sheet</u>				
<u>Assets:</u>				
Available for sale securities	(a)	\$ 6,888	6,666	13,554
Permanent Investments	(a)	9,556	(6,666)	2,890
Deferred Taxes	(b)	775	246	1,021
Other assets	(b)	<u>1,137</u>	<u>3</u>	<u>1,140</u>
		\$ 18,356	249	18,605
		=====	=====	=====
<u>Liabilities:</u>				
Income taxes	(c)	\$ 336	(7)	329
Payable ESPS	(c)	271	(2)	269
Sundry creditors and other accounts payable	(b)	<u>865</u>	<u>725</u>	<u>1,590</u>
		\$ 1,472	716	2,188
		=====	=====	=====
<u>Stockholders' equity</u>				
Earned capital:				
Retained earnings	(c)	\$ 2,720	75	2,795
Remeasurements of defined employees' benefits	(b)	-	(574)	(574)
Net income	(c)	<u>1,321</u>	<u>32</u>	<u>1,353</u>
		\$ 4,041	(467)	3,574
		=====	=====	=====

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	<u>Balance previously reported</u>	<u>Restatment adjustments</u>	<u>Restated balances</u>
<u>Statement of income:</u>			
Interest Income	\$ 21,187	4	21,191
Other operation (expenses) income	141	(4)	137
Administrative and promotion expenses	(3,181)	2	(3,179)
Current income taxes	<u>(824)</u>	<u>30</u>	<u>(794)</u>
	\$ 17,323	32	17,355
	=====	=====	=====
<u>Statement of cash flow:</u>			
Net income	\$ 1,321	32	1,353
Current and deferred tax	545	(30)	515
Others	136	(715)	(579)
Change in other operating assets	(20,774)	(3)	(20,777)
Change in other operating liabilities	<u>(166)</u>	<u>716</u>	<u>550</u>
	\$ (18,938)	-	(18,938)
	=====	=====	=====

- (a) Reclassification of net equity investments (stock securities) of the subsidiary *Corporación Mexicana de Inversiones de Capital, S.A. de C.V.*
- (b) Recognition of the remeasurements of defined employees' benefits in the OCI (see numeral (c) of this note).
- (c) Recognition of account receivable of tax return of *Fideicomiso venta de títulos en directo al público* and difference in tax payment for 2016.

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(5) Foreign currency position -

Central Bank regulations require that banks maintain balanced positions in foreign currencies within certain limits. The short or long position permitted by the Central Bank is equal to a maximum of 15% of the basic capital computed as of the third immediately preceding quarter. Therefore, as of December 31, 2017 and 2016, the Institution's position is within the authorized limits. The foreign currency position is analyzed as follows:

	<u>Dollars</u>		<u>Equivalent in pesos</u>	
	<u>2017</u>	<u>2016</u>	<u>2017</u>	<u>2016</u>
Assets	8,006	6,186	\$ 157,428	127,575
Liabilities	(8,144)	(6,188)	(160,146)	(127,620)
Short position	(138)	(2)	\$ (2,718)	(45)
	=====	=====	=====	=====

At December 31, 2017 and 2016, the assets and liabilities in millions of foreign currency of domestic currency and valued balances are shown below:

Domestic currency:

	<u>2017</u>			<u>2016</u>
	<u>Assets</u>	<u>Liabilities</u>	<u>Net position</u>	<u>net position</u>
USD dollars	7,747	(7,895)	(148)	(6)
Japanese Yen	25,038	(25,037)	1	1
Euros	23	(22)	1	1
Sterling pounds	6	-	6	2
Special draft fees	1	-	-	-
			(140)	(2)
			=====	=====

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At December 31, 2017 and 2016, the assets and liabilities in foreign currencies valued in pesos are shown below:

	<u>2017</u>			<u>2016</u>
	<u>Assets</u>	<u>Liabilities</u>	<u>Net position</u>	<u>net position</u>
USD dollars	\$ 152,326	(155,240)	(2,914)	(110)
Japanese yen	4,372	(4,372)	-	-
Euros	548	(512)	36	15
Sterling pounds	168	(8)	160	50
Special draft fees	<u>14</u>	<u>(14)</u>	<u>-</u>	<u>-</u>
	<u>\$ 157,428</u>	<u>(160,146)</u>	<u>(2,718)</u>	<u>(45)</u>

The exchange rate relative to the US dollar at December 31, 2017 and 2016, was \$19.6629 pesos per dollar and \$20.6194 pesos per dollar, respectively, and on the authorization issuance date of the consolidated financial statements was \$18.4797 pesos per dollar.

(6) Cash and cash equivalents-

At December 31, 2017 and 2016, the caption is integrated as follows:

	<u>2017</u>	<u>2016</u>
Domestic and foreign banks	\$ 14,573	13,243
Call money	3,020	2,800
24 and 48 hours foreign currency sales	(2,353)	(19,743)
Other funds available (due on demand)	1	1
Restricted funds:		
Deposits with the central bank	13,082	13,079
24, 48 and 72 hours foreign currency purchase	<u>228</u>	<u>6,318</u>
	<u>\$ 28,551</u>	<u>15,698</u>

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December 31, 2017 and 2016, deposits at the Central Bank correspond to monetary regulation deposits of \$13,082 and \$13,079, respectively, which have no maturity. The interest generated by deposits in the Central Bank at December 31, 2017 and 2016, were \$889 and \$572, respectively. The Provisions in force issued by the Central Bank for monetary regulation deposits set that may be comprised of cash, securities, or both.

December 31, 2017 and 2016, the Institution had the following call money:

	2017			2016		
	Amount	Annual rate	Term	Amount	Annual rate	Term
Central Bank	\$ 2,770	7.25%	4 days	\$ -	-	-
Sociedad Hipotecaria Federal, S. N. C.	250	1.42%	4 days	665	0.68%	2 days
Banco Invex, S. A.	-	-	-	73	5.75%	2 days
Bancomext, S. N. C.	-	-	-	<u>2,062</u>	0.68%	2 days
	\$ <u>3,020</u>			\$ <u>2,800</u>		

At December 31, 2017 and 2016, foreign currency receivable and deliverable equivalent in pesos in connection with the purchases and sales to be settled within 24, 48 and 72 hours were negotiated in USD dollars.

At December 31, 2017 and 2016, cash and cash equivalent in foreign currency are as follows:

<u>2017</u>	Millions of domestic currency	Exchange rate	Equivalent in pesos
USD dollars	640	\$ 19.66290	\$ 12,593
Euros	2	23.60629	57
Sterling pounds	1	26.60489	<u>26</u>
			\$ 12,676
			<u><u>=====</u></u>

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<u>2016</u>	<u>Millions of domestic currency</u>	<u>Exchange rate</u>	<u>Equivalent in pesos</u>
US Dollars	43	20.61940	\$ 879
Euros	3	21.75347	67
Sterling Pounds	2	25.48145	<u>47</u>
			\$ 993
			<u>=====</u>

At December 31, 2017 and 2016, the losses from operations of buy/sell currencies amounted to \$(2,914) and \$(5,101), respectively.

(7) Investment securities-

At December 31, 2017 and 2016, investment securities at fair value, except held to maturity, are analyzed as follows:

Trading:

	<u>2017</u>			<u>2016</u>
	<u>Acquisition cost</u>	<u>Accrued interest</u>	<u>Valuation</u>	<u>Book Value</u>
Fondo de Desarrollo para el Mercado de Valores (FDMV)	\$ 287	-	(19)	268
Bonds	1,787	8	8	1,803
Certificates	4,784	17	5	4,806
CETES	79	1	-	80
Ipabonos	5,556	62	17	5,635
Bank Promissory notes	<u>632</u>	<u>-</u>	<u>-</u>	<u>632</u>
Subtotal carried forward:	\$ <u>13,125</u>	<u>88</u>	<u>11</u>	<u>13,224</u>
				<u>26,810</u>

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	2017			2016	
	Acquisition cost	Accrued interest	Valuation	Book value	
Subtotal					
brought forward:	\$ <u>13,125</u>	<u>88</u>	<u>11</u>	<u>13,224</u>	<u>26,810</u>
Restricted securities:					
Bonds	71,413	44	193	71,650	88,263
Certificates	14,244	9	(11)	14,242	14,197
CETES	-	-	-	-	230
Ipabonos	92,217	97	86	92,400	89,208
Bank promissory notes	2,770	1	(21)	2,750	1,519
Investment securities placed in guarantee:					
Ipabonos	3	-	-	3	34
Equity investments	<u>203</u>	<u>-</u>	<u>-</u>	<u>203</u>	<u>-</u>
	<u>\$ 193,975</u>	<u>239</u>	<u>258</u>	<u>194,472</u>	<u>220,261</u>
<u>Available for sale:</u>					
	2017			2016	
	Acquisition cost	Accrued interest	Valuation	Book value	
Sovereign debt	\$ 2,249	29	68	2,346	3,146
Bonds issued by credit Institution	236	2	6	244	252
Debentures and other securities	4,181	72	53	4,306	3,490
Securities issued by foreign entities	194	1	-	195	-
Equity investments	<u>6,932</u>	<u>-</u>	<u>1,064</u>	<u>7,996</u>	<u>6,666</u>
	<u>\$ 13,792</u>	<u>104</u>	<u>1,191</u>	<u>15,087</u>	<u>13,554</u>

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Held-to-maturity:

	2017			2016
	Acquisition cost	Accrued interest	Book value	Book value
<u>Securities</u>				
Convertible prizes bonds	\$ 5	-	5	5
Certificates	215	137	352	338
Segregable certificates	2,286	961	3,247	1,554
Sovereign debt	258	6	264	187
Debenture and other securities	1,192	15	1,207	1,160
Udibonos	51	20	71	67
Restricted securities:				
Segregable certificates	<u>5,905</u>	<u>2,494</u>	<u>8,399</u>	<u>9,560</u>
Total	\$ <u>9,912</u>	<u>3,633</u>	<u>13,545</u>	<u>12,871</u>

An analysis by maturity term of the integration of trading securities for trading purposes, considering the acquisition cost:

Trading securities-

2017	Less than a month	Between one and three months	More than three months	Without term	Total
Acciones del Fondo de Desarrollo para el Mercado de Valores (FDMV)	\$ -	-	-	287	287
Bonds	-	3	1,784	-	1,787
Certificates	64	-	4,720	-	4,784
CETES	28	18	33	-	79
Ipabonos	<u>40</u>	<u>-</u>	<u>5,516</u>	<u>-</u>	<u>5,556</u>
Subtotal carried forward	\$ <u>132</u>	<u>21</u>	<u>12,053</u>	<u>287</u>	<u>12,493</u>

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<u>2016</u>	<u>Less than a month</u>	<u>Between one and three months</u>	<u>More than three months</u>	<u>Without term</u>	<u>Total</u>
Subtotal brought forward:	\$ <u>15,141</u>	<u>4</u>	<u>11,540</u>	<u>109</u>	<u>26,794</u>
Restricted securities	-	-	88,239	-	88,239
Certificates	14,223	-	-	-	14,223
CETES	230	-	-	-	230
Ipabonos	-	-	89,099	-	89,099
Bank promissory notes	1,518	-	-	-	1,518
Securities placed in guarantee:					
Ipabonos	<u>-</u>	<u>-</u>	<u>34</u>	<u>-</u>	<u>34</u>
	<u>\$ 31,112</u>	<u>4</u>	<u>188,912</u>	<u>109</u>	<u>220,137</u>
	=====	==	=====	===	=====

Available-for-sale -

<u>Securities</u>		<u>More than a year</u>	
		<u>2017</u>	<u>2016</u>
Sovereign debt	\$	2,249	3,172
Bonds issued by credit institutions		236	204
Debentures and other securities		3,775	3,548
Securities issued by foreign entities		194	-
Equity investments		<u>6,932</u>	<u>5,760</u>
	\$	<u>13,386</u>	<u>12,684</u>
		=====	=====

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At December 31, 2017, the Institution holds debentures and securities that amounts to \$406 with less than one-year term.

Held-to-maturity:

<u>2017</u>		<u>Less than a year</u>	<u>More than a year</u>	<u>Total</u>
Prides convertible bonds	\$	-	5	5
Certificates		17	198	215
Segregable certificates		-	2,286	2,286
Sovereign debt		-	258	258
Debentures and other securities		304	888	1,192
Udibonos		-	51	51
Restricted securities: Segregable certificates		<u>-</u>	<u>5,905</u>	<u>5,905</u>
Total	\$	<u>321</u>	<u>9,591</u>	<u>9,912</u>
<u>2016</u>				
Prides convertible bonds	\$	-	5	5
Certificates		268	-	268
Segregable certificates		-	1,167	1,167
Sovereign debt		-	183	183
Debentures and other securities		87	1,056	1,143
Udibonos		-	51	51
Restricted securities: Segregable certificates		<u>-</u>	<u>7,175</u>	<u>7,175</u>
Total	\$	<u>355</u>	<u>9,637</u>	<u>9,992</u>

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The valuation result from available for sale securities as of December 31, 2017, and 2016 recognized in Other Comprehensive Income within stockholders' equity amounted to \$108 and \$(178), net of deferred income tax, respectively.

For the years ended December 31, 2017 and 2016, net gains from interest income, trading income and valuation income from investments securities are as follows:

	<u>2017</u>	<u>2016</u>
Interest income	\$ 2,946	1,725
Valuation result	167	186
Trading income	127	541
	=====	=====

For the years ended December 31, 2017 and 2016, the Institution has not made reclassifications from held to maturity to available for sale, or from trading securities to available for sale.

Issuers over 5% of institution's net capital-

At December 31, 2017, investments in non-governmental debt securities of the same issuer and exceeding 5% of the Institution's net capital are analyzed below:

<u>Issuer</u>	<u>Series</u>	<u>Number of securities</u>	<u>Annual average rate</u>	<u>Average term</u>	<u>Amount</u>
FEFA	Various	165,520,000	7.45%	569	\$ 15,689
SHF	14001	14,993,409	6.08%	781	1,473
PEMEX	Various	138,200	5.05%	1,795	2,948
		=====			=====

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(8) Securities on repurchase/resell agreements -

At December 31, 2017, and 2016 the “Debtors on repurchase/resell agreements” and “Creditors on repurchase/resell agreements” balances in which the Institution acts as repurchase or as repurchaser, are analyzed as follows:

	Debtors on repurchase/resell agreements		Creditors on repurchase/resell agreements	
	<u>2017</u>	<u>2016</u>	<u>2017</u>	<u>2016</u>
Government securities:				
Udibonos	\$ -	-	(1,965)	-
Segregable certificates	-	-	(8,077)	(9,344)
Bonds	12,555	16,331	(64,536)	-
Fix rate bonds	2,001	12	(4,956)	(88,262)
Ipabonos	850	5,934	(92,315)	(89,127)
Cetes	<u>-</u>	<u>20</u>	<u>-</u>	<u>(230)</u>
Subtotal	<u>15,406</u>	<u>22,297</u>	<u>(171,849)</u>	<u>(186,963)</u>
Banking securities:				
Certificates	-	-	(15,747)	(14,226)
Banks promissory notes	<u>-</u>	<u>-</u>	<u>(1,172)</u>	<u>(1,500)</u>
	<u>-</u>	<u>-</u>	<u>(16,919)</u>	<u>(15,726)</u>
Collateral sold or pledged as a guarantee (creditors)				
Bonds	(9,837)	(16,331)	-	-
Fix rate bonds	(2,001)	(12)	-	-
Ipabonos	<u>(850)</u>	<u>(5,934)</u>	<u>-</u>	<u>-</u>
	<u>(12,688)</u>	<u>(22,277)</u>	<u>-</u>	<u>-</u>
Debtors (creditors) on repurchase/resell agreements	\$ <u>2,718</u>	<u>20</u>	<u>(188,768)</u>	<u>(202,689)</u>

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At December 31, 2017 the terms of resell/repurchase agreements, vary between 1 and 84 days (1 and 180 days at December 31, 2016) with annual weighted rates of 7.42% acting as repurchase and 7.41% acting as repurchaser in 2017.

During the years ended December 31, 2017 and 2016, interest income amounted to \$15,286 and \$10,097, respectively; interest expense amounted to \$14,781 and \$9,057, respectively, and are included in the consolidated income statement under the caption of "Interest income" and "Interest expense", respectively.

(9) Derivatives-

At December 31, 2017 and 2016, the fair value of derivative financial instruments for trading and hedging purposes, recognized under the caption "Derivatives", is analyzed as follows:

<u>2017</u>	<u>Assets</u>	<u>Liabilities</u>	<u>Balance</u>	
			<u>Debit</u>	<u>(Credit)</u>
Trading purposes:				
Forward contracts	\$ 84,078	(82,667)	1,411	-
Valuation	<u>(316)</u>	<u>790</u>	<u>474</u>	<u>-</u>
	<u>83,762</u>	<u>(81,877)</u>	<u>1,885</u>	<u>-</u>
Swaps	<u>55,854</u>	<u>(55,934)</u>	<u>-</u>	<u>(80)</u>
Total	\$ <u>139,616</u>	<u>(137,811)</u>	<u>1,885</u>	<u>(80)</u>
Hedging purposes:				
Swaps	\$ <u>38,870</u>	<u>(46,575)</u>	<u>-</u>	<u>(7,705)</u>

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<u>2016</u>	<u>Assets</u>	<u>Liabilities</u>	<u>Balance</u>	
			<u>Debit</u>	<u>(Credit)</u>
Trading purposes:				
Futures	\$ 2	(2)	-	-
Valuation	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
	<u>2</u>	<u>(2)</u>	<u>-</u>	<u>-</u>
Forward contracts	64,023	(64,069)	(46)	-
Valuation	<u>(35)</u>	<u>263</u>	<u>228</u>	<u>-</u>
	<u>63,988</u>	<u>(63,806)</u>	<u>182</u>	<u>-</u>
Swaps	<u>54,460</u>	<u>(54,511)</u>	<u>-</u>	<u>(51)</u>
Total	\$ 118,450	(118,319)	182	(51)
	=====	=====	===	=====
Hedging purposes:				
Swaps	\$ 33,728	(43,232)	-	(9,504)
	=====	=====	===	=====

The Institution participates in the mexican derivatives market (MEXDER), through trading of interest rates and currency futures, in accordance with the authorization granted by Central Bank.

In the case of over-the-counter dollar-peso forwards, the master agreement does not establish maintaining guarantees, instead it does apply penalties on the nonperforming counter party. The interest rate futures and exchange rate forwards contracts carried out by the Institution are oriented to obtain earnings for the Institution.

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In the case of dollar-peso forward for trading purposes, the fair value represents the amount that two parties agree to exchange, based on sources of information that affect the prices of these operations.

The Institution performs various analyses on underlying markets over derivative instruments that are traded on the market in order to identify and assess the risks implied in the Institution's position through the Risk Management Committee. Operations with futures and forward contracts, involve recovery risks. To reduce the risks in the operation of these instruments, the institution maintains matched positions.

Futures and forward contracts:

Trading purposes:

	<u>2017</u>	<u>2016</u>
Sales:		
Contract value	\$ 82,667	64,069
	=====	=====
Receivable	\$ 81,877	63,806
	=====	=====
Purchases:		
Contract value	\$ 84,078	64,023
	=====	=====
Deliverable	\$ 83,762	63,988
	=====	=====
Valuation	\$ 474	228
	=====	=====

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Swaps:

Trading purposes:

		<u>Contract</u> <u>value</u>	<u>Receivable</u>	<u>Deliverable</u>	<u>Net</u> <u>position</u>
<u>2017</u>					
Interest rate	\$	172,462 =====	55,854 =====	55,934 =====	(80) ==
<u>2016</u>					
Interest rate	\$	133,392 =====	54,460 =====	54,511 =====	(51) ==

Hedging purposes:

		<u>Contract</u> <u>value</u>	<u>Receivable</u>	<u>Deliverable</u>	<u>Net</u> <u>position</u>
2017	\$	84,844 =====	38,870 =====	46,575 =====	(7,705) =====
2016	\$	81,016 =====	33,728 =====	43,232 =====	(9,504) =====

At December 31, 2017 and 2016, hedge effectiveness/ineffectiveness derived from the application of the B-5 criterion "Derivatives and hedging transactions" of the Banking Commission, is detailed in the following page.

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Fair value hedge Swaps (applicable to results):

		<u>2017</u>	<u>2016</u>
Valuation for:			
Certificates	\$	(9)	(48)
Deposit certificates		-	<u>6</u>
Total	\$	(9)	(42)
		==	==

At December 31, 2017 and 2016, the Institution has only contracted swaps designated at fair value hedge.

Trading Swaps (applicable to results):

		<u>2017</u>	<u>2016</u>
Interest rate	\$	(80)	(51)
		==	==

The adjustments to book value arising from interest rate hedges on financial assets and liabilities, due to the application of the criterion B-5 "Derivatives and hedging transactions" of the Banking Commission, at December 31 2017 and 2016, are detailed below:

	<u>2017</u>		<u>2016</u>	
	<u>Assets</u>	<u>Liabilities</u>	<u>Assets</u>	<u>Liabilities</u>
Certificates	\$ 15,251	(11,150)	(5,291)	(8,256)
Bank promissory notes	-	-	(55)	(60)
Loan	<u>43</u>	<u>(53)</u>	<u>5,417</u>	<u>4,617</u>
Total	\$ 15,294	(11,203)	71	(3,699)
	=====	=====	=====	=====

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The net gain (loss), for the years ended December 31, 2017 and 2016, recognized in the consolidated income statement derived from the ineffectiveness of instruments used for fair value hedging purposes, amounted to \$31 and \$3,473, respectively. The effect of gain related to the effective hedge portion for the year ended December 31, 2017 and 2016 amounted to \$18 and \$29, respectively.

At December 31, 2017 and 2016, the gain from valuation of fair value hedging derivatives was \$587 and \$1 respectively; while the loss from valuation of the hedged item related to the hedged risk was (\$582) and \$(7), respectively.

Use of derivative financial instruments policy management-

The Institution's policies allow the use of derivative instruments for hedge and trading purposes. The main objectives of the operation of these instruments is risk hedging and generation of revenues that support the Institution's profitability. The establishment of objectives and policies related to the operation of these instruments are included in the Risk Management regulatory and operational manuals.

Derivative financial instruments used by the Institution are interest and exchange rate swaps, IPC and interest rate futures, as well as exchange rate forwards, which, according to the portfolio, can support hedging and trading strategies.

Derivative financial instruments are traded on over-the-counter markets and recognized stock markets. Eligible counterparties for the OTC derivatives are mainly domestic and foreign banks, whereas derivatives traded in stock markets, the clearing houses are the counter parties.

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Processes and levels of authorization-

Control processes, policies and levels of authorization for transactions with derivatives are set forth in the Integral Risk Management Committee (IRMC), whose duties include approval of:

1. The specific limits for discretionary risks, when it has been empowered 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, measure, overseeing, limit, controlling, reporting and disclosing the different 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 Risk Management area, must concur with the Institution's technology.
4. The methodologies for identifying, valuation, measurement 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 Risk Management area.
6. The evaluation of matters of Risk Management referred to in Article 77 of the Provisions for its presentation to the Board of Directors and the Banking Commission.
7. The 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 relation with any line of business are approved by the Committee, in accordance with the powers granted by the Board of Directors.

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Independent reviews-

The Institution is under the supervision and monitoring of the Banking Commission and the Central Bank, which is performed through processes of monitoring, inspection visits, requirements of information and documentation, and delivery of reports. There are also periodic reviews by the internal and external auditors.

Generic description on valuation techniques-

Derivative financial instruments are valued in accordance with the criterion B-5 "Derivatives and hedging transactions" issued by the Banking Commission.

Valuation methodology-

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

The internal and external sources of liquidity used to meet requirements related to derivative financial instruments are national and international treasury (London Branch).

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

Stress tests and backtesting are performed on regular basis to estimate the impact on derivatives instruments positions and to validate statistically that the measurement of market risk models provide results consistent with the exposure to the market variability, which must be maintained within the parameters approved by the IRMC.

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The methodology currently used for preparing stress measurement report, consists of calculating the current portfolio value, having ability to apply changes in risk factors occurring in:

- Tequila Effect (1994)
- Russian Crisis (1998)
- Twin Towers (2001)
- Mexican Stock Exchange Effect (2002)
- Effect on Real Interest Rate (2004)
- Mortgage Crisis Effect (2008)
- USA Elections effect (2016).

Backtesting tests are based on the daily generation of the following information:

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

During 2017, the number of derivative financial instruments traded was the following:

Instrument		<u>Number of transactions</u>		<u>Notional</u>	
		<u>Trade</u>	<u>Hedge</u>	<u>Trade</u>	<u>Hedge</u>
Futures	(1)	350	-	60,284	-
Forwards (Arbitrations)	(2)	216	-	23,828	-
Swaps	(3)	83	109	67,930	26,797
		===	===	=====	=====

- (1) The number of transactions is equal to the transactions of purchase less sales. Notional refers to number of contracts: 30,317 of purchase and 29,967 sales.
- (2) Purchasing transactions. Notional in millions of US dollars.
- (3) Notional amount traded during the year.

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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 Banking Commission), the Institution has a hedge file that includes the following information:

1. File cover letter.
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. Derivative confirmation.

Sensitivity analysis-

A sensitivity analysis is performed through different measures every day, such as:

1. Duration.- There are primarily two types of duration with different meanings:
 - 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.
 - Modified Duration: It is the percentage variation experienced by the price of a bond in light of 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.

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3. Greeks- Sensitivity measurements for options, except for interest rate options:
- a) Delta: Price Sensitivity for options at the price of the underlying 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 of the option.
 - d) Vega: Price Sensitivity of the option in response to volatility used for its valuation.
 - e) Rho: Price Sensitivity of the option in response to changes in 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 there in, in order for it to govern its criterion in taking the risk with these instruments.

(10) Loan portfolio-

(a) Classification of loan portfolio by currency

At December 31, 2017 and 2016, the classification of loans into current and past due by currency (valued in local currency), is analyzed as follows:

	2017			2016		
	Local Currency	Foreign Currency	Total	Local Currency	Foreign Currency	Total
Current:						
Business or commercial activity	\$ 16,368	35,365	51,733	19,050	40,832	59,882
Financial institutions	149,820	8,780	158,600	124,786	9,543	134,329
Government entities	16,045	22	16,067	17,656	32	17,688
Consumer loans	8	-	8	8	-	8
Mortgage loans	119	-	119	134	-	134
Loans granted as agent of the Federal Government	-	65	65	-	94	94
Subtotal carried forward:	\$ <u>182,360</u>	<u>44,232</u>	<u>226,592</u>	<u>161,634</u>	<u>50,501</u>	<u>212,135</u>

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	2017			2016		
	<u>Local currency</u>	<u>Foreign currency</u>	<u>Total</u>	<u>Local currency</u>	<u>Foreign currency</u>	<u>Total</u>
Subtotal brought forward:	\$ 182,360	44,232	226,592	161,634	50,501	212,135
Past due:						
Business or commercial activity	-	575	575	-	602	602
Financial institutions	1,284	-	1,284	1,560	-	1,560
Consumer loans	2	-	2	4	-	4
Mortgage loans	<u>6</u>	<u>-</u>	<u>6</u>	<u>12</u>	<u>-</u>	<u>12</u>
	<u>1,292</u>	<u>575</u>	<u>1,867</u>	<u>1,576</u>	<u>602</u>	<u>2,178</u>
Total	\$ <u>183,652</u>	<u>44,807</u>	<u>228,459</u>	<u>163,210</u>	<u>51,103</u>	<u>214,313</u>

Loans granted by the Institution acting as a financial agent, corresponds to financing granted to Federal Government entities with resources obtained from international organizations for this particular purpose, which are presented in the loan portfolio.

Loans to financial institutions are granted to banking and non-banking entities through the discount of documents from individuals and entities engaged in business activities.

At December 31 2017 and 2016, the Institution has no loan portfolio subject to support program promoted by the Federal Government.

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(b) Classification of loan portfolio by economic sector -

At December 31, 2017 and 2016, credit risk, classified by economic sector and the percentage of concentration are analyzed as follows:

	<u>2017</u>		<u>2016</u>	
	<u>Amount</u>	<u>%</u>	<u>Amount</u>	<u>%</u>
Federal Government	\$ 87	0.03	125	0.06
Decentralized agencies and state-owned enterprises	11,540	5.05	8,720	4.07
State productive enterprises	4,504	1.97	6,515	3.04
Commercial banks	53,890	23.59	53,372	24.90
Other public financial brokers	1,225	0.54	2,422	1.13
Other private financial brokers	104,771	45.86	88,078	41.10
Domestic companies	52,308	22.9	54,478	25.42
Private parties	134	0.06	158	0.07
Foreign financial entities	-	-	445	0.21
	<u>\$ 228,459</u>	<u>100</u>	<u>214,313</u>	<u>100</u>

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(c) Additional loan portfolio information -

Annual weighted lending rates (not audited):

During 2017 and 2016, annual weighted rates not audited, were as follows:

	<u>2017</u>	<u>2016</u>
Commercial loans*	8.27%	6.62%
Consumer	4.36%	4.62%
Mortgages	3.25%	2.10%
Excluded	2.54%	1.44%
	=====	=====

* Includes commercial, financial and government entities.

Restructured loans:

At December 31, 2017 and 2016, restructured and renewed loans are analyzed as follows:

<u>2017</u>	<u>Current</u> <u>portfolio</u>	<u>Past due</u> <u>portfolio</u>	<u>Total</u>
Commercial loans	\$ 46	-	46
Financial entities	<u>191</u>	<u>-</u>	<u>191</u>
	\$ 237	-	237
	====	=====	=====

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<u>2016</u>	<u>Current portfolio</u>	<u>Past due portfolio</u>	<u>Total</u>
Commercial loans	\$ 47	-	47
Financial entities	<u>280</u>	<u>-</u>	<u>280</u>
	\$ 327	-	327
	<u>===</u>	<u>====</u>	<u>====</u>

For the years ended December 31, 2017 and 2016, interests arising from restructured loans amounted to \$21 and \$18, respectively.

Current commercial loans renewed by the Institution during 2017 which continue being current amounted to \$4,923. During 2016, no renewed loans were carried out.

Risk Concentration:

At December 31, 2017, the Institution has twenty-three economic group debtors that exceeded 10% of its basic capital. The amount of funding to these groups is \$147,516, and represent 6 times the amount of basic capital as of September 2017. At December 31, 2016, the Institution had twenty-six group debtor that exceeded such limit totaling \$143,130 and represented 6.42 times the amount of the basic capital as of September, 2016. The balance of the loans granted to the three largest borrowers as of December 31, 2017 and 2016, amounts to \$55,752 and \$46,781, respectively.

Past-due portfolio:

An analysis of past-due loans at December 31, 2017 and 2016, from the date the loans were considered past due are summarized in next page.

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	<u>1 to 180</u> <u>days</u>	<u>181 to 365</u> <u>days</u>	<u>Over 2</u> <u>years</u>	<u>Total</u>
<u>2017</u>				
Commercial*	\$ -	-	1,859	1,859
Consumer	1	-	1	2
Mortgage	<u>4</u>	<u>1</u>	<u>1</u>	<u>6</u>
	\$ 5	1	1,861	1,867
	=====	=====	=====	=====
<u>2016</u>				
Commercial*	\$ -	-	2,162	2,162
Consumer	1	1	2	4
Mortgage	<u>2</u>	<u>-</u>	<u>10</u>	<u>12</u>
	\$ 3	1	2,174	2,178
	=====	=====	=====	=====

* Includes commercial, financial and government entities.

The movement in the past-due loan portfolio for the years ended December 31, 2017 and 2016, is summarized below:

	<u>2017</u>	<u>2016</u>
Balance at beginning of year	\$ 2,178	1,894
Settlements	(8)	(337)
Write-offs	(275)	-
Transfer from performing to nonperforming portfolio	-	621
Foreign exchange fluctuation	<u>(28)</u>	<u>-</u>
	\$ 1,867	2,178
	=====	=====

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At December 31, 2017 and 2016 the past-due loan portfolio is comprised of 38 former employees and 2 companies, which are on judicial or extra-judicial process.

The interests on the past due loan portfolio not recognized in results amounted to \$263 for year ended December 31, 2017 (\$268 in 2016), which are recorded in memorandum accounts.

For the years ended December 31, 2017 and 2016, the Institution recorded write-offs from those past due loans that had been fully reserved, for a total of \$275 and \$146, respectively.

The effect derived from suspension of the accrual interest of the nonperforming loans, represented a decrease that amounts to \$22 compared to 2016, as consequence from adjustments to balances recognized due to borrowers that went into commercial bankruptcy.

For the years ended December 31, 2017 and 2016, the Institution had no recoveries from write off loans.

Impaired, loan portfolio:

In accordance with criterion B-6, "Loan portfolio", of the Provisions, commercial loans, are deemed impaired loan when it is determined that, based on current facts and information, as well as the review process of such loans, there is a significant likelihood of not being entirely recovered, in accordance with the terms and conditions originally agreed. Both the current and non-performing portfolio may be identified as an impaired portfolio.

At December 31, 2017 and 2016, the impaired portfolio is summarized below:

<u>2017</u>		<u>Risk grade</u>			<u>Allowance recorded</u>
		<u>D</u>	<u>E</u>	<u>Total</u>	
Current	\$	235	-	235	106
Past-due		-	<u>1,859</u>	<u>1,859</u>	<u>1,521</u>
Total	\$	<u>235</u>	<u>1,859</u>	<u>2,094</u>	<u>1,627</u>

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<u>2016</u>		<u>Risk grade</u>			<u>Allowance recorded</u>
		<u>D</u>	<u>E</u>	<u>Total</u>	
Current	\$	47	-	47	21
Past due		-	<u>2,162</u>	<u>2,162</u>	<u>1,496</u>
Total	\$	<u>47</u>	<u>2,162</u>	<u>2,209</u>	<u>1,517</u>

Interest and commissions from loans at December 31, 2017 and 2016, are integrated as follows:

<u>2017</u>	<u>Interest</u>	<u>Commissions from loans granted</u>	<u>Total</u>
Business or commercial activity	\$ 2,577	37	2,614
Financial institutions	10,189	42	10,231
Government entities	1,085	-	1,085
Mortgage loans	4	-	4
Consumer loans	1	-	1
Credits granted as			
Federal Government			
Financial agent	<u>2</u>	<u>-</u>	<u>2</u>
	\$ <u>13,858</u>	<u>79</u>	<u>13,937</u>

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<u>2016</u>	<u>Interest</u>	<u>Commissions From loans granted</u>	<u>Total</u>
Business or commercial activity	\$ 2,114	39	2,153
Financial institutions	6,014	55	6,069
Government entities	716	-	716
Mortgage loans	2	-	2
Credits granted as			
Federal Government			
financial agent	<u>3</u>	<u>-</u>	<u>3</u>
	\$ 8,849	94	8,943
	=====	==	=====

The average weighted term for the amortization of commissions collected by granting loans is on monthly basis.

Adjustment from valuation of financial asset hedging:

The fair value hedges of interest rate risk of a portion of a portfolio comprised of financial assets, could generate an adjustment to the carrying amount of the hedged item, the gain or loss is recorded in the consolidated income statement and is presented under valuation adjustments for hedging financial assets.

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At December 31, 2017 and 2016, the adjustment to the carrying value of the loan portfolio from the gain or loss recognized in results of operations for the year is presented under the caption "Valuation adjustment from hedging of financial assets" in the consolidated balance sheet for \$15,294 and \$71, respectively.

(d) Allowance for loan losses-

At December 31, 2017 and 2016, as a result from the application of the allowance for loan losses methodology, the probability of default and loss given default by type of loan portfolio, obtained as weighted average (not audited) from the exposure at default, are as follows:

<u>Type of loan portfolio</u>	<u>Probability of default</u>	<u>Loss given default</u>	<u>Exposure at default</u>
<u>2017</u>			
Commercial	2.42%	45.02%	\$ 302,205
Mortgage	7.99%	17.62%	125
Consumer	27.30%	83.28%	10
Exempted	-	-	65
	=====	=====	=====
<u>2016</u>			
Commercial	2.45%	45.18%	\$ 277,670
Mortgage	11.01%	26.16%	146
Consumer	40.60%	73.48%	12
Exempted	-	-	94
	=====	=====	=====

The parameters are weighted on the loans of each of the portfolios. Exposure at default shown for credit includes credit commitments.

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In accordance with the provisions for the loan portfolio rating, for development banking institutions, loan portfolio under the responsibility of the Federal Government and taking in discount to development banking entities, is not subject to the creation of allowance for loan losses, since these entities assume the credit risk. The balances of the loan portfolio and contingent operations subject to rating are controlled in memorandum accounts are evaluated based on the methodologies established by the Banking Commission.

At December 31, 2017, the credit rated loan portfolio and allowance for loan losses, are analyzed as follows:

Credit rated portfolio

<u>Grade of Risk</u>	<u>Business commercial</u>	<u>Financial institutions</u>	<u>Government entities</u>	<u>Consumer</u>	<u>Mortgage</u>	<u>Total</u>
A-1	\$ 105,762	63,939	16,067	1	95	185,864
A-2	9,882	66,137	-	2	10	76,031
B-1	2,414	6,878	-	1	3	9,296
B-2	1,542	23,218	-	1	-	24,761
B3	1,042	2,841	-	1	5	3,889
C-1	27	300	-	1	4	332
C-2	13	22	-	-	4	39
D	231	27	-	1	2	261
E	<u>579</u>	<u>1,284</u>	<u>-</u>	<u>2</u>	<u>2</u>	<u>1,867</u>
Total	\$ <u>121,492</u>	<u>164,067</u>	<u>16,067</u>	<u>10</u>	<u>125</u>	<u>302,340</u>

Exempted portfolio:

Federal government 65

Total portfolio \$ 302,405

(Continued)

Nacional Financiera, S. N. C.,
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Allowance for loan losses:

<u>Grade of Risk</u>	<u>Business commercial</u>	<u>Financial institutions</u>	<u>Government entities</u>	<u>Consumer</u>	<u>Mortgage</u>	<u>Total</u>
A-1	\$ 515	363	80	-	-	958
A-2	109	807	-	-	-	916
B-1	39	114	-	-	-	153
B-2	38	499	-	-	-	537
B-3	30	103	-	-	-	133
C-1	2	21	-	-	-	23
C-2	2	2	-	-	1	5
D	100	12	-	-	-	112
E	<u>577</u>	<u>946</u>	<u>-</u>	<u>2</u>	<u>1</u>	<u>1,526</u>
Total	\$ <u>1,412</u>	<u>2,867</u>	<u>80</u>	<u>2</u>	<u>2</u>	<u>4,363</u>
Additional reserves recognized by the Banking Commission						536
Allowance for assignment of lines						<u>2,117</u>
Total						\$ <u>7,016</u>

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At December 31, 2016, the credit rated loan portfolio and the allowance for loan losses, are analyzed as follows:

Credit rated portfolio

<u>Grade of Risk</u>	<u>Business commercial</u>	<u>Financial institutions</u>	<u>Government entities</u>	<u>Consumer</u>	<u>Mortgage</u>	<u>Total</u>
A-1	\$ 101,788	69,583	17,573	-	101	189,045
A-2	6,668	47,531	-	-	12	54,211
B-1	3,843	15,170	-	-	5	19,018
B-2	7,457	617	117	3	1	8,195
B-3	124	4,663	-	2	6	4,795
C-1	6	231	-	-	1	238
C-2	14	-	-	3	3	20
D	105	-	-	-	9	114
E	<u>621</u>	<u>1,560</u>	<u>-</u>	<u>4</u>	<u>7</u>	<u>2,192</u>
Total	\$ <u>120,626</u>	<u>139,355</u>	<u>17,690</u>	<u>12</u>	<u>145</u>	<u>277,828</u>
Exempted portfolio:						
Federal government						<u>94</u>
Total portfolio						\$ <u>277,922</u>

Allowance for loan losses:

<u>Grade of Risk</u>	<u>Business commercial</u>	<u>Financial institutions</u>	<u>Government entities</u>	<u>Consumer</u>	<u>Mortgage</u>	<u>Total</u>
A-1	\$ 534	489	87	-	-	1,110
A-2	81	521	-	-	-	602
B-1	60	273	-	-	-	333
B-2	164	13	3	-	-	180
B-3	4	170	-	-	-	174
C-1	-	14	-	-	-	14
C-2	2	-	-	-	-	2
D	41	-	-	-	1	42
E	<u>284</u>	<u>1,222</u>	<u>-</u>	<u>4</u>	<u>7</u>	<u>1,517</u>
Subtotal	\$ <u>1,170</u>	<u>2,702</u>	<u>90</u>	<u>4</u>	<u>8</u>	<u>3,974</u>
Additional reserve recognized by the Banking Commission						865
Allowance for assignment of lines						<u>800</u>
Total						\$ <u>5,639</u>

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The movement in the allowance for loan losses for the years ended December 31, 2017 and 2016 is summarized as follows:

	<u>2017</u>	<u>2016</u>
Balance at beginning of year	\$ 5,639	4,703
Provision charged to results of year	2,638	1,532
Application, write-offs and others	(287)	(146)
Allowance cancellation	(930)	(581)
Exchange rate fluctuations	<u>(44)</u>	<u>131</u>
Balance at end of year	\$ <u>7,016</u>	<u>5,639</u>

(11) Other accounts receivable, net-

At December 31, 2017 and 2016, other accounts receivable, are shown below:

	<u>2017</u>	<u>2016</u>
Loans to Institution's personnel	\$ 2,659	2,489
Clearing accounts	2,272	13,424
Other receivables	800	874
Receivables for fees on current trading activities	93	96
Payments receivable on swap trades	<u>11,402</u>	<u>9,618</u>
	17,226	26,501
Allowance for write-offs of other receivables	<u>(665)</u>	<u>(604)</u>
Total	\$ <u>16,561</u>	<u>25,897</u>

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**Nacional Financiera, S. N. C.,
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(12) Foreclosed assets -

At December 31, 2017 and 2016, foreclosed assets are analyzed as follows:

	<u>2017</u>	<u>2016</u>
Premises	\$ 30	31
Furniture, securities and foreclosed rights	<u>30</u>	<u>32</u>
	60	63
Allowances for impairment	<u>(56)</u>	<u>(54)</u>
	\$ 4	9
	==	==

The movement of the allowance for impairment for the years ended December 31, 2017 and 2016 is analyzed as follows:

	<u>2017</u>	<u>2016</u>
Balance at beginning of year	\$ (54)	(51)
Additional provisions due to aging charged to operations for the year	(2)	(6)
Credit to income on sale of foreclosed assets and write-offs	<u>-</u>	<u>3</u>
Balance at end of year	\$ (56)	(54)
	==	==

In conformity with the Provisions, additional reserves has been recorded for foreclosed assets in judicial or extra-judicial process or received in lieu of payment.

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(13) Premises, furniture and equipment -

Premises, furniture and equipment at December 31, 2017 and 2016 are analyzed as follows:

	<u>2017</u>			<u>2016</u>
	<u>Cost</u>	<u>Investment</u> <u>Restated</u>	<u>Total</u>	<u>Total</u>
Office premises	\$ 310	1,941	2,251	2,241
Furniture and equipment	143	97	240	243
Computer equipment	24	4	28	30
Land	<u>9</u>	<u>-</u>	<u>9</u>	<u>9</u>
Subtotal	486	2,042	2,528	2,523
Accumulated depreciation	(241)	(801)	(1,042)	(1,021)
Total	\$ <u>245</u>	<u>1,241</u>	<u>1,486</u>	<u>1,502</u>

The useful lives during which main assets are depreciated are shown below:

Useful life

Office premises	53 to 70 years
Furniture and equipment	10 years
Computer equipment	3 to 4 years

Depreciation charged to results of operations for the years ended December 31, 2017, and 2016 amounted to \$35 and \$38, respectively.

For the years ended December 31, 2017 and 2016, there was no effect from impairment of improvements and adaptations.

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According to assessment carried out by the Institution, the residual value (except land) at December 31, 2017 and 2016 is minimum.

(14) Permanent investments -

At December 31, 2017 and 2016, the permanent investment, are integrated as follows:

	<u>2017</u>	<u>2016</u>
Corporación Andina de Fomento	\$ 2,578	2,692
Shares of other entities	<u>229</u>	<u>133</u>
	2,807	2,825
Investment of subsidiary companies:	<u>29</u>	<u>26</u>
Total	\$ <u>2,836</u>	<u>2,851</u>

At December 31, 2017 and 2016, the other permanent investments are integrated as follows:

	<u>2017</u>	<u>2016</u>
Fideicomiso Asistencia Técnica en Programas de Financiamiento PYME	\$ 14	16
Fideicomiso Patronato del Centro de Diseño de México	14	15
Fideicomiso Capital Emprendedor	4	4
Fideicomiso al Mercado Intermedio de Valor	-	3
Fideicomiso Eurocentro Nafin-México	<u>-</u>	<u>1</u>
Total	\$ <u>32</u>	<u>39</u>

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The movement in the permanent investments and other permanent investments at December 31, 2017 is summarized as follows:

Balance at beginning of year	\$	2,890
Equity method in the results of unconsolidated subsidiaries and affiliates		6
Exchange translation		(111)
Investments acquisition		123
Investments disposal		<u>(40)</u>
Balance at end of year	\$	<u>2,868</u> =====

(15) Deposit funding -

At December 31, 2017 and 2016, the deposit-funding caption is analyzed as follows:

	<u>2017</u>			<u>2016</u>		
	<u>Currency</u>			<u>Currency</u>		
	<u>Domestic</u>	<u>Foreign</u>	<u>Total</u>	<u>Domestic</u>	<u>Foreign</u>	<u>Total</u>
Time deposits:						
Money market	\$ <u>72,147</u>	<u>62,149</u>	<u>134,296</u>	<u>104,897</u>	<u>38,573</u>	<u>143,470</u>
Debt securities issued:						
Stock certificates	57,595	-	57,595	51,367	-	51,367
Bank bonds	-	40,670	40,670	-	28,622	28,622
Securities notes	<u>-</u>	<u>14,246</u>	<u>14,246</u>	<u>-</u>	<u>10,352</u>	<u>10,352</u>
	<u>57,595</u>	<u>54,916</u>	<u>112,511</u>	<u>51,367</u>	<u>38,974</u>	<u>90,341</u>
Total deposit funding	\$ <u>129,742</u>	<u>117,065</u>	<u>246,807</u>	<u>156,264</u>	<u>77,547</u>	<u>233,811</u> =====

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At December 31, 2017 and 2016, time deposits from the money market according to their maturity are integrated as follows:

	<u>2017</u>	<u>2016</u>
Less than one year	\$ 128,756	143,075
Between one and five years	<u>5,153</u>	<u>153</u>
	133,909	143,228
Accrued interest	<u>387</u>	<u>242</u>
	\$ <u>134,296</u>	<u>143,470</u>

The not audited average weighted interest rates and average terms in days on time deposits from money market are as follows:

(a) Time deposits from money market -

<u>Instrument</u>	<u>Annual average rate</u>	<u>Average term in days</u>	<u>Amount</u>
Stock certificates	7.99	2,780	\$ 5,153
Bank promissory notes	7.11	7	66,618
Deposit certificates in foreign currency (valued)	0.24	15	<u>62,138</u>
			133,909
Accrued interest			<u>387</u>
			\$ <u>134,296</u>

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**Nacional Financiera, S. N. C.,
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(16) Debt securities issued in the country-

December 31, 2017 and 2016, the Institution has issued stock certificates with par value of one hundred pesos, under the financial program authorized by the Ministry of finance, as shown below:

<u>Issuance date</u>	<u>Maturity</u>	<u>Securities (millions)</u>	<u>Par value (pesos)</u>	<u>Interest rate</u>	<u>2017</u>	<u>2016</u>
CEBURES:						
03/08/2012	22/07/2022	20	100	5.69	\$ 2,000	2,000
10/12/2012	22/07/2022	20	100	5.69	2,000	2,000
22/11/2013	08/03/2024	30	100	6.55	3,000	3,000
14/03/2014	08/03/2024	47.5	100	6.55	4,750	4,750
06/06/2014	02/06/2017	20	100	3.24	-	2,000
06/06/2014	08/03/2024	40	100	6.55	4,000	4,000
26/09/2014	02/06/2017	17.5	100	3.24	-	1,750
26/09/2014	08/03/2024	32.5	100	6.55	3,250	3,250
17/04/2015	07/03/2025	60	100	6.15	6,000	6,000
17/04/2015	13/04/2018	10	100	3.23	1,000	1,000
24/08/2015	13/04/2018	30	100	3.48	3,000	3,000
24/08/2015	07/03/2025	40	100	6.15	4,000	4,000
10/04/2017	03/04/2020	47.5	100	7.44	4,750	-
12/04/2017	25/09/2026	12.5	100	6.2	1,250	-
	Premium or discount on placement				(127)	(35)
	Accrued interest payable				615	571
					<u>39,488</u>	<u>37,286</u>
CEBURES payable Euroclear and Clearstream						
25/04/2016	17/04/2019	10	100	4.05	1,000	1,000
27/04/2016	25/09/2025	50	100	6.20	5,000	5,000
21/10/2016	17/04/2019	18	100	5.52	1,800	1,800
25/10/2016	25/09/2026	42	100	6.20	4,200	4,200
	Premium or discount on placement				(88)	(94)
	Accrued interest payable				138	135
					<u>12,050</u>	<u>12,041</u>
	Subtotal carried forward				\$ <u>51,538</u>	<u>49,327</u>

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<u>Issuance date</u>	<u>Maturity</u>	<u>Securities (millions)</u>	<u>Par value (pesos)</u>	<u>Interest rate</u>	<u>2017</u>	<u>2016</u>
Subtotal brought forward				\$	<u>51,538</u>	<u>49,327</u>
Green bond denominated in domestic currency						
02/09/2016	01/09/2023	20	100	6.05	2,000	2,000
Accrued interest payable					<u>38</u>	<u>40</u>
					<u>2,038</u>	<u>2,040</u>
Social bond						
21/07/2017	15/07/2022	40	100	7.37	4,000	-
Accrued interest payable					<u>19</u>	<u>-</u>
					<u>4,019</u>	<u>-</u>
Total					\$ <u>57,595</u>	<u>51,367</u>

In April 2016, were issued two stock certificates (fixed-rate and reviewable rate) under the communicative units format and under the program of syndicated auctions that the Institution has been carrying out since the end of 2013. However, there was a new feature for the fixed-rate tranche, since the necessary formalities were carried out for that instrument to be settled through Euroclear or Clearstream, allowing the participation of foreign investors and seeks to increase the investors base.

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Additionally, in November 2016, the Institution issued its second green bond, through a transaction in the local market, denominated in pesos and with a seven years term. The placement had diversification of investors, which positioned the Institution again as a leading in this type of initiatives to promote the transition toward a competitive, sustainable economy and low carbon emissions. The demand was close to \$6,000 (2.92. times) and the final placement amounted to \$2,000 which was initially used to finance three projects, two mini-hydroelectric plants and an eolian park located in Nayarit and Puebla, respectively. The issuance was also highlighted by the support of the second opinion from Sustainalytic. This marks the beginning of Green bonds in Mexico since it is the first issue in pesos of this type.

In July 2017, the Institution placed the first social bond listed in the Mexican Stock Exchange. The demand of this transaction amounted to \$13,373 (3.34 times) and the final placement amounted to \$4,000 and 6.68 times the target amount that was \$2,000. The placement rate had a difference compared with TIIE rate of 28 days less 2 points basis with a term of 5 years. The rating for this placement was AAA (or its equivalent) at local level by 5 rating agencies S & P, Moody's, Fitch, DBRS and HR.

Institution's social bond is aligned with the social bonds principles 2017 of the International Capital Market Association ("ICMA"), due to the nature of the eligibility criteria for the programs and populations target. Additionally, contributes to the objectives of development sustainable (ODS) of the United Nations, in order to reduce the poverty, inclusive education, gender equality, worthy employment and sustainable and inclusive economic growth. The social bond had a second opinion from Sustainalytics B.V., firm provider of research and analysis of environmental and social governance which evaluated the instrument to ensure that it is aligned with social bonds principles.

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Valuation adjustments of hedging financial liabilities

The fair value hedges of interest rate risk of a portion of a portfolio comprised of financial liabilities could generate an adjustment to the carrying amount of the hedged item, the gain or loss is recorded in the consolidated income statement and is presented under valuation adjustments for hedging financial liabilities.

At December 31, 2017 and 2016, the loss (gain) recognized in results of operations for the year is presented under the caption "Valuation adjustment from hedging of financial liabilities" in the consolidated balance sheet for \$11,203 and (\$3,699), respectively.

(17) Credit securities issued abroad-

Bank bonds:

At December 31, 2017 and 2016, the bank bonds balance amounts to \$40,670 and \$28,622, respectively. The current balances of securities placed by the Institution abroad, as shown below:

2017

<u>Currency</u>	<u>Securities</u>	<u>Balance in foreign currency</u>	<u>Interest</u>	<u>% Average rate</u>	<u>Balance in local currency</u>	<u>term</u>
US dollars	120	1,889	4	1.37323	\$ 37,222	less than one year
	6	174	1	1.58250	<u>3,448</u>	over one year
					\$ 40,670	
					=====	

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2016

<u>Currency</u>	<u>Securities</u>	<u>Balance in foreign currency</u>	<u>Interest</u>	<u>% Average rate</u>	<u>Balance in local currency</u>	<u>term</u>
US dollars	87	1,237	2	1.05351	\$ 25,544	less than one year
	4	149	-	1.64825	<u>3,078</u>	over one year
					\$ 28,622	
					<u><u>28,622</u></u>	

Stock notes:

At December 31, 2017 and 2016, the current balance of this caption for \$14,246, and \$10,352, respectively, is integrated as follows:

<u>Currency</u>	<u>Balance in foreign currency (millions)</u>	<u>% Average Rate</u>	<u>Balance in local currency</u>	<u>Term</u>
<u>2017</u>				
US dollars	500	3.375	\$ 9,831	5 years
Japanese yen	10,000	0.78	1,746	5 years
Japanese yen	15,000	0.66	2,620	5 years
Premium or discount on placement			(8)	
Accrued interest			<u>57</u>	
			\$ 14,246	
			<u><u>14,246</u></u>	

2016

US dollars	500	3.375	\$ 10,310	5 years
Premium or discount on placement			(12)	
Accrued interest			<u>54</u>	
			\$ 10,352	
			<u><u>10,352</u></u>	

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(18) Bank and other borrowings -

At December 31, 2017 and 2016, bank and other borrowings are comprised as follows:

	<u>2017</u>	<u>2016</u>
Multinational and governmental agencies:		
World Bank	\$ 983	1,031
Inter-American Development Bank	7,080	7,540
Others	<u>4,025</u>	<u>5,904</u>
	12,088	14,475
Banking institutions	5,285	10,143
Other borrowings	8,003	5,699
Accrued interest	<u>25</u>	<u>33</u>
	\$ <u>25,401</u>	<u>30,350</u>

At December 31, 2017 and 2016, maturity term less than one year amount to \$12,816 and \$19,039, respectively.

At December 31, 2017, bank and other borrowings maturity dates are integrated in next page.

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**Nacional Financiera, S. N. C.,
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<u>Financial Agency</u>	<u>Average rate</u>	<u>Average term to maturity (residual)</u>	<u>Millions in foreign currency</u>	<u>Local currency</u>
Due on demand				
Local currency	7.15	2 days	8,003	\$ 8,003
Interest			<u>3</u>	<u>3</u>
Total			<u>8,006</u>	\$ <u>8,006</u>
Short term				
Us dollars:				
Commercial banking	1.7633	122 days	29	\$ 576
NF BID Cclip 2226 oc	2.3300	166 days	5	98
Me desarrollo	2.3300	135 days	2	49
Instituto de Crédito Oficial	1.3333	120 days	1	20
Corporación Andina de Fomento	1.5681	19 days	200	3,933
Euros:				
Commercial banking	1.4588	341 days	<u>3</u>	<u>78</u>
Subtotal carried forward				\$ <u>4,754</u>

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<u>Financial Agency</u>	<u>Average rate</u>	<u>Average term to maturity (residual)</u>	<u>Millions in foreign currency</u>	<u>Local currency</u>
Subtotal brought forward				\$ 4,754
Financial agent				
Euros:				
Inter-American Development Bank	3.0000	102 days	1	20
Special draft fees:				
International Agricultural Development Fund	2.0800	213 days	-	14
Interest			1 ==	22 ==
Total				\$ 4,810 =====

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<u>Financial Agency</u>	<u>Average rate</u>	<u>Average term to maturity (residual)</u>	<u>Millions in foreign currency</u>	<u>Local currency</u>
Long term				
US dollars:				
Commercial banking	2.1671	9 years/10 months	218	\$ 4,285
Instituto Comercial de Crédito	1.3333	3 years/3 months	3	59
NF BID Cclip oc Me Desarrollo Pymes Pemex	2.3300	17 years/5 months	83	1,622
NF ctf BIRF 98062 Programa de Sustitución de electrodomésticos	0.7500	12 years/8 months	50	983
2631 tc Me Programa de Financiamiento de Energías Renovables	0.7500	14 years/6 months	70	1,376
NF BID Cclip/oc-Me Programa Línea de Créditos Condiciona Me-x1010	2.3300	20 years/4 months	98	1,917
NF BID 3237/oc-Me Programa Financiamiento Impulso Cogeneración	2.3300	22 years/5 months	100	1,966
Euros:				
Commercial banking	1.4220	4 years/9 months	15	346
Financial agent				
Euro:				
Inter-American Development Bank Washington DC	3.0000	2 years/3 months	1	31
Total			====	\$ 12,585 =====

(Continued)

Nacional Financiera, S. N. C.,
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Notes to the Consolidated Financial Statements

(Millions of pesos, except where stated different)

At December 31, 2016 bank and other borrowings maturity dates are integrated as follows:

2016

<u>Financial Agency</u>	<u>Average rate</u>	<u>Average term to maturity (residual)</u>	<u>Millions in foreign currency</u>	<u>Local currency</u>
Due on demand				
Local currency	5.7167	1 day	5,699	\$ 5,699
Interest			<u>1</u>	<u>1</u>
Total				\$ 5,700 =====
Short term				
US dollars:				
Commercial banking	1.3646	53 days	355	\$ 7,306
NF BID Cclip 2226 oc				
Me Desarrollo	2.1400	161 days	5	103
Instituto de Crédito Oficial	1.3333	120 days	1	21
Corporación Andina de Fomento	1.1004	31 days	<u>280</u>	<u>5,773</u>
				<u>13,203</u>
Euros:				
Commercial banking	1.4588	341 days	<u>3</u>	<u>71</u>
Financial agent				
Euros:				
Inter-American Development Bank Washington, D.C.	3.000	112 days	<u>1</u>	<u>19</u>
Special draft fees:				
International Agricultural Development Fund	1.3100	212 days	-	<u>14</u>
Subtotal carried forward			<u>-</u>	\$ <u>14</u>

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<u>Financial Agency</u>	<u>Average rate</u>	<u>Average term to maturity (residual)</u>	<u>Millions in foreign currency</u>	<u>Local currency</u>
Subtotal brought forward			-	\$ <u>14</u>
Interest			<u>2</u>	<u>32</u>
Total				\$ <u>13,339</u>
Long term				
US dollar:				
Commercial banking	2.0511	5 years 6 months	42	\$ 862
Instituto Comercial de Crédito	1.3333	9 years/18 years	77	1,595
NF BID Cclip oc Me Desarrollo				
Pymes Pemex	2.1400	6 months/13 years	88	1,804
NF ctf BIRF 98062 Programa de Sustitución de Electrodomésticos	0.7500	9 months/15 years	50	1,031
2631 tc Me Programa de Financiamiento de Energías Renovables	0.7500	15 years/7 months	70	1,443
NF BID Cclip/oc-Me Programa Línea de Créditos Condiciona Me-x1010	2.1400	21 years/5months	100	2,062
NF BID 3237/oc-Me Programa Financiamiento Impulso Cogeneración	2.1400	23 years/6 months	100	<u>2,062</u>
Subtotal carried forward				\$ <u>10,859</u>

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<u>Financial Agency</u>	<u>Average rate</u>	<u>Average term to maturity (residual)</u>	<u>Millions in foreign currency</u>	<u>Local currency</u>
Subtotal brought forward				\$ <u>10,859</u>
Euros:				
Commercial banking	1.4220	6 years	<u>18</u>	<u>391</u>
Financial agent				
Euros:				
Inter-American Development Bank Washington, D.C.	3.0000	2 years/4 months	<u>2</u>	<u>47</u>
Special Draft fees:				
International Agricultural Development Fund	1.3100	1 year/8 months	<u>-</u>	<u>14</u>
Total				\$ <u>11,311</u> <u>=====</u>

The accounts of credits obtained not drawn down (note 23f) represents the lines of credit granted to the Institution not exercised at year-end, is analyzed as follows:

	<u>2017</u>	<u>2016</u>
Central Bank	\$ 210	535
Kreditanstalt für Wiederaufbau Frankfurt	760	701
Banco Interamericano de Desarrollo	<u>1,687</u>	<u>1,769</u>
Total	\$ <u>2,657</u> <u>=====</u>	<u>3,005</u> <u>=====</u>

(Continued)

**Nacional Financiera, S. N. C.,
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Notes to the Consolidated Financial Statements

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(19) Other accounts payable-

At December 31, 2017 and 2016, caption is analyzed as follows:

	<u>2017</u>	<u>2016</u>
Payables for cash collateral received	\$ 1,109	1,126
Sundry creditors	1,235	782
Employee benefits	306	725
Income taxes payable	253	329
Employee statutory profit sharing payable	275	269
Creditors on settlement of transactions	-	88
Other accounts payable	125	80
Deposits on guarantees	<u>3</u>	<u>3</u>
Total	\$ 3,306	3,402
	<u>=====</u>	<u>=====</u>

(20) Employees' benefits -

a) Defined - contribution retirement plan

Beginning in 2006, the Institution amended General Labour Conditions (GLC) based on trends and best practices in the management and operation of retirement and pension schemes, to incorporate new employees, as well as those who decided to migrate from defined benefits to defined contribution scheme. This scheme allows for having a greater control over costs and liabilities of the plan, maintain an adequate cost-benefit ratio for the Institution and for employees and establishes clear rules of contribution or retirement.

This plan consists of the contributions carried out by the Institution to open individual accounts for each employee, which are divided in two sub accounts, denominated "A" and "B", respectively. It further consists of contributions carried out by the employee to the sub-account "B" and the returns generated by both subaccounts, which are jointly identified as the employee's individual account.

(Continued)

**Nacional Financiera, S. N. C.,
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Notes to the Consolidated Financial Statements

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The amount of the contributions for the year ended December 31, 2016, amounted to \$32. During the year 2017, the Institution did not carry out contributions.

At December 31, 2017 and 2016, the defined contribution plan assets amounts to \$281 and \$269, respectively, and are invested in an irrevocable trust incorporated in the Institution.

b) Defined benefits retirement plan

Moreover, GECs set forth that employees who reach 65 years of age and complete 30 years of service will be entitled for a retirement annuity. Moreover, upon reaching 65 years of age with 5 years of seniority, employees will be entitled 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 the employee who has reached 60 years of age or completed 26 years of service.

On the other hand, the articles of the GEC dated August 12, 1994 set forth that employee who joined the Institution prior to the above mentioned 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 entitled for a pension in the terms of the GEC referred to above.

In the event of an unjustified dismissal or termination of the employment relationship, the employee may choose to receive the compensation upon termination or a retirement annuity calculated based on the main characteristics of the retirement plan if the employee is 50 years old and has 16 or more years of seniority.

Article 5 paragraph a) of the GEC, reviewed in 2006, establishes that individuals who have obtained pension for disablement, disability or retirement prior to this GEC review and those employees who joined the Institution prior to such date and to whom the defined retirement benefit plan applies, will continue to enjoy the right to receive from the Institution at the time when they retire the following additional benefits:

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- Short-term loans, medium-term loans and special loan for savings, which will be paid with a charge to caption “Administrative and promotional 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 monthly deductions from the short and medium-term loans with principal and interest multiplied by 72 months, with a 41.66% cap of monthly net pension. The special loan for Savings will bear 1% annual interest on the principal, which will be withheld by the Institution.

The net periodic cost for the years ended December 31, 2017 and 2016, amounts to \$960 and \$901, respectively, including the effect of other post-retirement benefits. The estimated net periodic cost for the year 2018 amounts to \$784.

At December 31, 2017 and 2016, the plan assets of the fund for labor obligations amounted to \$6,790 and \$6,511 respectively, and is invested in an irrevocable trust incorporated in the Institution. The net periodic cost recognized in the non-consolidated statement of income of the Institution amounted to \$331 and \$298, respectively.

In accordance with the provisions of MFRS D-3 employees’ benefits, the Institution recognized in the consolidated financial statements at December 31, 2017 and 2016 plan assets related to "other post-retirement benefits" for \$10,589 and \$9,941 respectively. Moreover, the net periodic cost recognized in the Institution’s results amounted to \$629 and \$603, respectively.

At December 31, 2017 and 2016, the assets of the plan of the Fund for labor obligations, is invested in the following securities:

Classification of securities in the Fund and its concentration.

	<u>2017</u>	<u>2016</u>
Government securities	29.85%	36.40%
Banking securities	11.14%	5.75%
Other debt securities	<u>59.01%</u>	<u>57.85%</u>
Total	100.00%	100.00%
	=====	=====

(Continued)

**Nacional Financiera, S. N. C.,
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Notes to the Consolidated Financial Statements

(Millions of Mexican pesos)

The summary of the actuarial calculations at December 31 2017, is as follows:

<u>Concept</u>	<u>Pension</u> <u>Retirement</u>	<u>Seniority</u> <u>premium</u> <u>Retirement</u> <u>and</u> <u>termination</u>	<u>Other</u> <u>retirement</u> <u>benefits</u> <u>Retirement</u>	<u>Special loan</u> <u>for savings</u> <u>(SLS) and</u> <u>financial</u> <u>credit cost</u> <u>Retirement</u>
Accounting policy for the recognition of losses and gains	Deferred amortization			
General benefits description	According to general employment conditions			
Obligation for acquired benefits	\$ 6,826 =====	7 =	7,987 =====	3,300 =====

Reconciliation between the value of the Defined Benefits Obligation (DBO) and the fair value plan assets (PA) with the net liability for defined benefits or net asset for defined benefits

Defined benefits obligations	\$(7,299)	(28)	(9,839)	(3,857)
Plan assets at fair value	<u>6,774</u>	<u>27</u>	<u>7,431</u>	<u>3,180</u>
Financial situation of the obligation	(525)	(1)	(2,408)	(677)
Remeasurements pending of recognition	<u>885</u>	<u>3</u>	<u>1,804</u>	<u>613</u>
Net (liability) asset for defined benefits	\$ 360 =====	2 ==	(604) =====	(64) =====

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**Nacional Financiera, S. N. C.,
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Notes to the Consolidated Financial Statements

(Millions of Mexican pesos)

<u>Concept</u>	<u>Pension</u> <u>Retirement</u>	<u>Seniority</u> <u>premium</u> <u>Retirement</u> <u>and</u> <u>termination</u>	<u>Other</u> <u>retirement</u> <u>benefits</u> <u>Retirement</u>	<u>Special loan</u> <u>for savings</u> <u>(SLS) and</u> <u>financial</u> <u>credit cost</u> <u>Retirement</u>
Net (liability) assets for defined benefits at the beginning of year	\$ 296	(4)	640	(179)
Net periodic cost	329	2	470	159
Contributions	(329)	(2)	(470)	(159)
Adjustment for recognition of differences in the reserve	56	1	(12)	22
Remeasurements of liabilities or (assets) recognized in OCI	(712)	1	(24)	221
Net (liability)/ asset for defined benefits	\$ (360)	(2)	604	64
	====	==	=====	====

(Continued)

**Nacional Financiera, S. N. C.,
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Notes to the Consolidated Financial Statements

(Millions of Mexican pesos)

Concept	<u>Pension</u>	<u>Seniority</u>	<u>Other</u>	<u>Special loan</u>
	<u>Retirement</u>	<u>premium</u>	<u>retirement</u>	<u>for savings</u>
		<u>retirement</u>	<u>benefits</u>	<u>(SLS) and</u>
		<u>and</u>		<u>financial</u>
		<u>termination</u>	<u>Retirement</u>	<u>credit cost</u>
			<u>Retirement</u>	<u>Retirement</u>
Net periodic cost				
Labor cost	\$ 29	2	152	37
Financial cost	497	2	609	231
Return on assets	(420)	(2)	(457)	(200)
Recycling of remeasurements	<u>223</u>	-	<u>166</u>	<u>91</u>
Net period cost	\$ <u>329</u>	<u>2</u>	<u>470</u>	<u>159</u>
	====	=	====	====
Net liability (asset) reameasurements for defined benefits				
Defined benefits obligations	\$ 7,299	28	9,839	3,857
Estimated defined benefits obligation	<u>7,954</u>	<u>26</u>	<u>9,928</u>	<u>3,698</u>
Actuarial (gains) / losses on obligations	\$ (655)	2	(89)	159
	=====	==	=====	=====

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**Nacional Financiera, S. N. C.,
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(Millions of Mexican pesos)

Concept	<u>Pension Retirement</u>	<u>Seniority premium Retirement and termination</u>	<u>Other retirement benefits Retirement</u>	<u>Special loan for savings (SLS) and financial credit cost Retirement</u>
Fair value of the plan assets	6,774	27	7,431	3,180
Estimated value of plan assets	<u>6,828</u>	<u>27</u>	<u>7,525</u>	<u>3,239</u>
(Gains) / losses on return on plan assets	<u>54</u>	<u>-</u>	<u>94</u>	<u>59</u>
Remeasurements generated in the year to recognize in OCI	\$ (601) =====	2 ==	5 =====	218 =====
Average remaining working life	6.26	11.20	15.50	6.26

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**Nacional Financiera, S. N. C.,
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Notes to the Consolidated Financial Statements

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Main hypothesis used:

	<u>2017</u>	<u>2016</u>
Discount rate	7.00%	6.50%
Increase in wage rate	4.00%	4.00%
Increase of minimum wage rate	4.00%	3.50%
Medical inflation rate	9.50%	9.50%
Long term inflation rate	3.50%	3.50%

(a) Actuarial values were determined by Bufete Matemático Actuarial, S.C. considering the hypothesis at December 31, 2017.

(b) The hypothesis as of December 31, 2016 were used to determine the 2017 net periodic.

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

<u>Concept</u>	<u>Pension Retirement</u>	<u>Seniority premium Retirement and termination</u>	<u>Other retirement benefits Retirement</u>	<u>Special loan for savings (SLS) and financial credit cost Retirement</u>
Accounting policy for the recognition of losses and gains			Deferred Amortization	
General benefits description			According to general labor conditions	
Obligation for acquired benefits	\$ 7,378 =====	5 ==	7,586 =====	2,979 =====

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**Nacional Financiera, S. N. C.,
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(Millions of Mexican pesos)

<u>Concept</u>	<u>Pension</u> <u>Retirement</u>	<u>Seniority</u> <u>premium</u> <u>Retirement</u> <u>and</u> <u>termination</u>	<u>Other</u> <u>retirement</u> <u>benefits</u> <u>Retirement</u>	<u>Special loan</u> <u>for savings</u> <u>(SLS) and</u> <u>financial</u> <u>credit cost</u> <u>Retirement</u>
Reconciliation between the value of the Defined Benefits Obligation (DBO) and the fair value plan assets (PA) with the net liability for defined benefits or net asset for defined benefits				
Defined benefits obligation	\$ (7,920)	(28)	(9,547)	(3,654)
Plan assets at fair value	<u>6,572</u>	<u>29</u>	<u>6,977</u>	<u>3,104</u>
Net (liability) / asset for defined benefits	(1,348)	1	(2,570)	(550)
Remeasurements pending of recognition	<u>1,052</u>	<u>4</u>	<u>1,930</u>	<u>730</u>
Net (liability)/ asset for defined benefits	\$ <u>(296)</u>	<u>5</u>	<u>640</u>	<u>180</u>
Reserve balance at beginning of year	\$ (56)	(1)	12	(22)
Net periodic cost	296	2	388	215
Contributions	(296)	(2)	(388)	(215)
Liability/(asset) remeasurements recognized in OCI	<u>352</u>	<u>(4)</u>	<u>628</u>	<u>(158)</u>
Net (liability) / asset For defined benefits (NLBD)/NADB)	\$ <u>296</u>	<u>(5)</u>	<u>640</u>	<u>(180)</u>

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Notes to the Consolidated Financial Statements

(Millions of Mexican pesos)

<u>Concept</u>	<u>Pension</u> <u>Retirement</u>	<u>Seniority</u> <u>premium</u> <u>Retirement</u> <u>and</u> <u>termination</u>	<u>Other</u> <u>retirement</u> <u>benefits</u> <u>Retirement</u>	<u>Special loan</u> <u>for savings</u> <u>(SLS) and</u> <u>financial</u> <u>credit cost</u> <u>Retirement</u>
Net periodic cost				
Labor Cost	\$ 33	2	140	33
Financial cost	458	2	531	231
Return on assets	(401)	(2)	(425)	(192)
Recycling of remeasurements	<u>206</u>	<u>-</u>	<u>142</u>	<u>143</u>
Net periodic cost	\$ <u>296</u>	<u>2</u>	<u>388</u>	<u>215</u>
Remeasurements for liability (asset) for defined benefits				
Defined benefits obligations	\$ 7,920	28	9,546	3,654
Estimated Defined benefits obligation	<u>7,562</u>	<u>29</u>	<u>8,995</u>	<u>3,862</u>
Actuarial (Gains) / losses on obligations	\$ <u>358</u>	<u>(1)</u>	<u>551</u>	<u>(208)</u>

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(Millions of Mexican pesos)

<u>Concept</u>	<u>Pension</u> <u>Retirement</u>	<u>Seniority</u> <u>premium</u> <u>Retirement</u> <u>and</u> <u>termination</u>	<u>Other</u> <u>retirement</u> <u>benefits</u> <u>Retirement</u>	<u>Special loan</u> <u>for savings</u> <u>(SLS) and</u> <u>financial</u> <u>credit cost</u> <u>Retirement</u>
Fair value of the plan assets	6,571	29	6,977	3,104
Estimated value of the plan assets	<u>6,565</u>	<u>26</u>	<u>7,054</u>	<u>3,155</u>
(Gains) / losses on return on plan assets	<u>(6)</u>	<u>(3)</u>	<u>77</u>	<u>51</u>
Remeasurements to recognize in OCI	\$ <u>352</u>	<u>(4)</u>	<u>628</u>	<u>(157)</u>
Average remaining working life	6.30	11.20	15.38	6.30
Main hypothesis used:				
		<u>2017</u>	<u>2016</u>	
Discount rate		6.50%	6.25%	
Increase in wage rate		4.00%	4.00%	
Increase of minimum wage rate		3.50%	3.50%	
Medical inflation rate		9.50%	9.00%	
Long term inflation rate		3.50%	3.50%	

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(Millions of Mexican pesos)

- (a) Actuarial values were determined by Bufete Matemático Actuarial, S.C. considering the hypothesis at December 31, 2016.
- (b) The hypothesis as of December 31, 2015 were used to determine the 2016 net periodic cost.

Financial Position

At December 31, 2017 and 2016, the financial position is as follows:

	Retirement pension plan	Seniority premium Retirement and termination	Other retirement benefits	
			Medical service, savings fund insurance, sport club	SLS and financial credit cost
<u>2017</u>	<u>Retirement</u>	<u>and termination</u>	<u>Retirement</u>	<u>Retirement</u>
Defined benefits obligation	\$ (7,299)	(28)	(9,839)	(3,857)
Fair value of the plan assets	<u>6,774</u>	<u>27</u>	<u>7,431</u>	<u>3,180</u>
Obligation's financial position	(525)	(1)	(2,408)	(677)
Remeasurements pending for recognition	<u>885</u>	<u>3</u>	<u>1,804</u>	<u>615</u>
Net (liability) / asset for defined benefits	\$ <u>(360)</u>	<u>(2)</u>	<u>(604)</u>	<u>(64)</u>

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(Millions of Mexican pesos)

	Retirement pension plan	Seniority Premium Retirement and termination	Other retirement benefits Medical service, savings fund insurance, sport club	SLS and financial credit cost
<u>2016</u>	<u>Retirement</u>	<u>termination</u>	<u>Retirement</u>	<u>Retirement</u>
Defined benefits obligations	(7,920)	(28)	(9,547)	(3,654)
Fair value of the plan assets	<u>6,572</u>	<u>29</u>	<u>6,977</u>	<u>3,104</u>
Obligation's financial position	1,348	1	(2,570)	(550)
Remeasurements pending for recognition	<u>1,052</u>	<u>4</u>	<u>1,930</u>	<u>730</u>
Net (liability) / asset for defined benefits	\$ (296)	5	(640)	180
	=====	==	=====	=====

OCI Reserve reconciliation

At December 31, 2017 and 2016, the reserve and ORI reconciliation are as follows:

	Retirement pension plan	Seniority Premium Retirement and termination	Other retirement benefits Medical service, savings fund insurance, sport club	SLS and financial credit cost
<u>2017</u>	<u>Retirement</u>	<u>termination</u>	<u>Retirement</u>	<u>Retirement</u>
Reserve balance at beginning of year	\$ 296	(5)	640	(179)
Net periodic cost	329	2	470	159
Contributions	(329)	(2)	(470)	(159)
Adjustment for recognition of differences in the reserve	56	2	(11)	22
Remeasurements liabilities or (assets) recognized in OCI	<u>(712)</u>	<u>1</u>	<u>(25)</u>	<u>221</u>
Balance at end of year	\$ (360)	(2)	604	64
	=====	=	=====	=====

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	Retirement pension plan	Seniority Premium Retirement and termination	Other retirement benefits Medical service, savings fund insurance, sport club	SLS and financial credit cost
<u>2017</u>	<u>Retirement</u>	<u>termination</u>	<u>Retirement</u>	<u>Retirement</u>
Accumulated OCI statement				
Balance at beginning of year pending of recognition in OCI	\$ 1,052	3	1,930	730
Recycling of remeasurements	<u>(167)</u>	-	<u>(126)</u>	<u>(116)</u>
Balance at end of year pending of recognition in OCI	\$ 885	3	1,804	614
	<u>=====</u>	<u>=</u>	<u>=====</u>	<u>=====</u>
Beginning balance recognized in OCI	\$ 352	(4)	628	(157)
Recycling of remeasurements	(56)	-	(41)	25
Actuarial (gain) / losses in obligations	(654)	3	(89)	159
(Gains) / losses in return on plan assets	54	-	94	58
Adjustment remeasurements for recognition of differences in the reserve	<u>(56)</u>	<u>(1)</u>	<u>12</u>	<u>(22)</u>
Balance at end of year recorded in OCI	\$ (360)	(2)	604	64
	<u>=====</u>	<u>=</u>	<u>=====</u>	<u>=====</u>
Net liabilities (assets) due to defined benefits at end of year	\$ (360)	(2)	604	64
	<u>=====</u>	<u>=</u>	<u>=====</u>	<u>=====</u>

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	Retirement pension plan	Seniority Premium Retirement and termination	Other retirement benefits	
			Medical service, savings fund insurance, sport club	SLS and financial credit cost
<u>2016</u>	<u>Retirement</u>	<u>Retirement</u>	<u>Retirement</u>	<u>Retirement</u>
Reserve balance at beginning of year	\$ (56)	(1)	11	(23)
Net periodic cost	296	2	388	215
Contributions	(296)	(2)	(388)	(215)
Remeasurements for liabilities or (assets) recognized in OCI	<u>352</u>	<u>(4)</u>	<u>629</u>	<u>(157)</u>
Balance at end of year:	\$ <u>296</u>	<u>(5)</u>	<u>640</u>	<u>(180)</u>
Accumulated OCI statement				
Balance at Beginning of year pending to recognized in OCI	1,258	4	2,071	872
Recycling of remeasurement	<u>(206)</u>	<u>-</u>	<u>(141)</u>	<u>(142)</u>
Balance at end of year recorded in OCI	\$ <u>1,052</u>	<u>4</u>	<u>1,930</u>	<u>730</u>
Beginning balance recognized in OCI	-	-	-	-
Actuarial (gain) / losses in obligations	358	(1)	551	(208)
(Gains) /losses in return on plan assets	<u>(6)</u>	<u>(3)</u>	<u>77</u>	<u>51</u>
Balance at end of year recognized in OCI	<u>352</u>	<u>(4)</u>	<u>629</u>	<u>(157)</u>
Net liability (asset) for defined benefits at end of year.	<u>296</u>	<u>(4)</u>	<u>640</u>	<u>(180)</u>

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In accordance with the amendments to the provisions published in the Official Federal Gazette on December 31, 2015, and with the effectiveness of the new MFRS D-3 issued by the CINIF, the Institution adopted the progressive application referred to third transitory article of the Provisions aforementioned

Based on the aforementioned, the recognition of the balances indicated in subparagraphs a) and b) of the paragraph 81.2 of MFRS D-3, the balance of modifications to the plan not yet recognized and the unrecognized accumulated balance for gains or losses the plan, respectively, will be recognized in fiscal year 2021 at the latest, recognizing 20% from its initial application and an additional 20% in each of the subsequent years, up to 100% within a maximum period of 5 years. The decision of the Institution to adopt the progressive application of the recognition of these balances, was communicated to the Banking Commission in a timely manner.

The accumulated balance of Plan losses not recognized, amounts to \$(3,306). The initial effects of the application of MFRS D-3 involve 20% of the accumulated balance of \$(661), amount which will be recognized, in the caption of "Remeasurements for defined benefits for employees" in earned capital. The amount remaining for \$(2,645) will be applied to in the subsequent years, within a maximum period of 5 years.

(21) Income taxes and employee statutory profit sharing (ESPS)-

IT Law effective as of January 1, 2014 establishes an IT rate of 30% for 2014 and later years. The current ESPS rate is 10%, for the years 2017 and 2016.

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At December 31, 2017, and 2016 current IT and ESPS expense is as follows:

	<u>2017</u>	
	<u>IT</u>	<u>ESPS</u>
Current IT:		
Institution	\$ (106)	(274)
Consolidated trusts	(644)	-
Management funds	(8)	-
Plaza Insurgentes	<u>(19)</u>	<u>-</u>
Current IT and ESPS	(777)	(274)
Deferred	<u>433</u>	<u>119</u>
	\$ <u>(344)</u>	<u>155</u>

For the year ended December 31, 2016, current and deferred IT amounted to (\$794) and \$279, respectively.

The Institution does not consolidate the tax result with its subsidiaries, thus the information presented below is for informational purposes only.

The Institution has not recognized a deferred tax liability, on the undistributed profits of subsidiaries and associated companies; the Institution currently does not expect these undistributed profits to be reinvested and taxable in the near future.

Deferred IT and ESPS:

The deferred tax asset at December 31 2017 and 2016, is analyzed in the next page.

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The following is an analysis of the effective tax rate of the Institution without subsidiaries for the fiscal year ended December 31, 2017:

	<u>Tax</u>	<u>IT</u>	<u>Effective</u>	<u>ESPS at</u>
	<u>base</u>	<u>at 30%</u>	<u>rate</u>	<u>10%</u>
<u>December 31, 2017</u>				
Operating income	\$ 1,502	(451)	(30%)	(150)
Allocation to current tax:				
Adjustment for inflation effects	(531)	159	11%	53
Mark to market of investment securities	(500)	150	10%	50
Non-deductible expenses	378	(113)	(8%)	(38)
Allowance for loan losses	377	(113)	(8%)	(38)
Current and deferred income tax	(370)	111	7%	37
Deduction of paid ESPS	(269)	81	5%	-
Others, net	<u>172</u>	<u>(52)</u>	<u>(3%)</u>	<u>(16)</u>
Current tax	<u>759</u>	(228)	<u>(16%)</u>	(102)
Tax effect of consolidated Trusts (see note 1) ⁽¹⁾		<u>122</u>		<u>(172)</u>
Income tax and ESPS	\$	<u>(106)</u>		<u>(274)</u>

- (1) In accordance with article 13 of the tax law, when business activities are carried out through a trust, the Institution acting as trustee will determine under the terms of title II of tax law, the result or the fiscal loss for such activities in each fiscal year and fulfill the obligations, including the obligation to make fiscal payments on behalf of trustees.

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	<u>Tax</u>	<u>IT</u>		
	<u>Base</u>	<u>Tax</u>	<u>Effective</u>	<u>ESPS at</u>
		<u>at 30%</u>	<u>rate</u>	<u>10%</u>
<i>Allocation to deferred tax:</i>				
<i>(IT 30% and ESPS%):</i>				
Mark to market of investment securities	497	(149)	(10%)	(50)
Provisions and others	8	(2)	-	-
Allowance for loan losses to be deductible	(2,194)	658	44%	219
Interest on derivative financial instruments (swaps)	737	(221)	(15%)	(74)
Others	<u>(237)</u>	<u>71</u>	<u>5%</u>	<u>24</u>
Deferred tax	<u>(1,189)</u>	<u>357</u>	<u>24%</u>	<u>119</u>
Income tax	\$ 430	129	8%	(155)
	=====	=====	=====	=====

Other considerations:

In accordance with Mexican tax law, the tax authorities may examine transactions carried out during the five years prior to the most recent income tax return filed.

According to the IT Law, corporations carrying out transactions with related parties, whether domestic or foreign, are subject to a limits and tax obligations, to certain requirements as to the determination of the transaction prices, since these prices must be similar to those that would be used in arm's-length transactions.

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(22) Stockholders' equity -

(a) At December 31, 2017 and 2016, the Institution's capital stock is comprised as follows:

	"Series A"		Nominal value pesos	Amount		Total
	Capital Contribution Certificates			"Series A"	"Series B"	
	"Series A"	"Series B"				
Subscribed capital	31,548,000	16,252,000	\$ 50	\$ 1,577	813	\$ 2,390
Unissued Capital	(7,868,728)	(4,053,586)	50	(393)	(203)	(596)
Subscribed and paid in capital	<u>23,679,272</u>	<u>12,198,414</u>	\$ 50	\$ <u>1,184</u>	<u>610</u>	1,794
						Increase from restatement
						<u>7,011</u>
						Total
						\$ <u><u>8,805</u></u>

The Institution's capital stock will be represented in 66% by "A" series and 34% by "B" series. The "A" series may only be subscribed by the Federal Government and "B" series by Mexican individuals or companies. At December 31, 2017 and 2016, the Federal Government owns 66% of the "A" series and the 33.9% of "B" series, in both years.

(b) Contributions for future capital stock increases-

At December 31, 2017 and 2016, its value amounts to \$5,700 and \$2,750, respectively.

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At its extraordinary meeting held on, December 13, 2017, the Board of Directors authorized the Management of the Institution, to carry out the necessary arrangements to request to the Federal Executive, through the Ministry of Finance and Public Credit (SHCP for its acronym in Spanish), an increase of capital stock amounting to \$2,950, required to be able to support the volume of operations and investment banking, which includes the investments of venture capital, as well as maintain a level of prudential capitalization for the year ended 2017, such increase was received in the month of December 2017.

(c) Paid stock premium-

This premium applies to payments made by holders of series "B" certificates. The balance of the premiums paid at December 31, 2017 and 2016 amounts to \$8,922 in both years.

(d) Statutory reserves-

The nominal value of these reserves at December 31, 2017 and 2016, amounts to \$314 in both years and its restated value amounts to \$1,730 in both years.

(e) Dividends declared -

The dividends paid to individuals and residents abroad shall be subject to an additional tax of 10%, which is considered final and must be withheld by entities that distribute such dividends. The rule applies only to dividends payment from earnings generated beginning January 1, 2014.

For the years ended December 31, 2017 and 2016 there was no dividends decree.

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**Nacional Financiera, S. N. C.,
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(f) Comprehensive income-

The comprehensive income reported in the consolidated statement of changes in stockholders' equity, represents the result of total activity during the year and includes the net income, the effect of the valuation of investments securities available for sale for \$108 and \$(178) at December 31, 2017 and 2016, respectively, as well as the effect on valuation in associated and affiliated companies and the remeasurements of defined employees' benefits for \$742 and \$(213) at December 31, 2017, respectively (\$640 and (\$574) at December 31, 2016, respectively).

(g) Restrictions on stockholders' equity-

The Credit Institutions Law requires an appropriation of 10% of net income for the year to statutory reserves until such reserves reach an amount equal to paid in capital stock.

The tax basis of stockholders contributions and retained earnings may be distributed to the stockholders are tax free. Distributions in excess of the tax bases are subject to income tax. At December 31, 2017, the Capital contribution account of the Institution (Cuenta de Capital de Aportación or CUCA, not audited) and the net taxable income account (Cuenta de Utilidad Fiscal Neta or CUFIN, not audited), amounted to \$51,442 and \$12,662, respectively.

The retained earnings of subsidiaries may not be distributed to the Institution's stockholders until dividends are collected.

(h) Capitalization (not audited)-

At December 31, 2017 and 2016, the Institution maintained a capitalization index in excess of 10.5% (14.46% and 13.26%, at December 31, 2017 and 2016, respectively), it is classified as category I in both years in accordance with article 220 of the Provisions, the capitalization index is calculated by applying certain percentages in accordance with the risk assigned pursuant to the rules established by Central Bank. The next sheet presents the Institution's capitalization information (capitalization index reported to the Central Bank and subject to its approval).

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(i) Basic and complementary capital-

The Institution's net capital consists of \$26,777 of basic capital and assets adjusted of risk of \$185,223. Pursuant to the application of the portfolio rating methodology, complementary capital is zero, which implies that net capital is equal to the basic capital, this is which in turn equal to fundamental capital.

(j) Adjusted for market risks-

Assets adjusted for market risks amount to \$54,016 and are equivalent to a capital requirement of \$4,321, which are integrated as follows:

	<u>Risk weighted assets</u>	<u>Capital requirement</u>
Exposed positions to market risk by risk factor:		
Transactions in Mexican pesos at nominal interests rates	\$ 12,880	1,030
Transactions with debt securities in pesos with premium and adjustable rates	5,022	402
Transactions in Mexican pesos at real rates or denominated in UDI's	14,632	1,171
Positions in UDI's or with returns referred to the INPC	145	12
Foreign currency transactions at nominal rates	4,730	378
Foreign currency positions or with exchange rate indexed returns	3,768	301
Equity positions or with returns indexed to the price of a single share or group of shares	<u>12,839</u>	<u>1,027</u>
Total market risk	\$ <u>54,016</u>	<u>4,321</u>

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(k) Assets adjusted for credit risks-

Assets adjusted for credit risk amount to \$122,949 and are equivalent to a capital requirement of \$9,836. Assets adjusted for risk related to borrowers and deposits amount to \$86,392, which are equivalent to a capital requirement of \$6,911, and are comprised as follows:

	<u>Risk weighted assets</u>	<u>Capital requirement</u>
Weighted assets subject to credit risk by risk group:		
Group III (weighted at 20%)	15,111	1,209
Group III (weighted at 50%)	3,615	289
Group III (weighted at 100%)	1,237	99
Group IV (weighted at 20%)	3,504	280
Group VI (weighted at 120%)	680	54
Group VII (weighted at 50%)	8,310	665
Group VII (weighted at 100%)	4,787	383
Group VII (weighted at 120%)	11,523	922
Group VII (weighted at 150%)	914	73
Group VII-B (weighted at 100%)	783	63
Group VII-B (weighted at 120%)	35,312	2,825
Group VIII (weighted at Group VI%)	5	-
Group VIII (weighted at Group VII%)	114	9
Group IX (weighted at 100%)	<u>497</u>	<u>40</u>
Total credit risk	<u>86,392</u>	<u>6,911</u>

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l) Assets adjusted for operational risks

Assets adjusted for operational risks amounted to \$8,258 and are equivalent to a capital requirement of \$661.

Weighted assets subject to operational risk		
<u>Used Method</u>	<u>Assets weighttd by risk</u>	<u>Capital Requirement</u>
Basic benchmark	\$ 8,258 =====	661 =====
	<u>Average market and credit risk requirement of the last 36 months</u>	<u>Annual average of positive net income for the past 36 months</u>
	\$ 12,042 =====	4,404 =====

The annex 1-O of the Provisions establishes the requirements for the disclosure of information relating to capitalization, which shall contain, in addition to those listed in the preceding subparagraphs, the following sections:

1. Net capital is presented in accordance with the international format of revelation contained in the document "Format of capital integration without considering regulatory adjustments".

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<u>Ref.</u>	<u>Tier 1 Common Stock (CET 1): Instruments and reserves</u>	<u>Amount</u>
1	Common shares that qualify for Tier 1 common stock plus its applicable premium	\$ 23,427
2	Prior year income	4,148
3	Other elements of comprehensive income (and other reserves)	<u>3,126</u>
6	Tier 1 common stock before regulatory adjustments	\$ 30,701 =====
	Tier 1 common stock: regulatory adjustments	
15	Defined benefits pension plan	\$ <u>14,218</u>
26	Domestic regulatory adjustments	-
A	Other elements of comprehensive income (and other reserves)	
D	Investments in multi-lateral agencies	644
F	Investments in capital risk	3,093
G	Investments in mutual funds	<u>187</u>
28	Total regulatory adjustments to tier 1 common stock	\$ 3,924 =====
29	Tier 1 Common Stock (CET 1)	\$ 26,777 =====
	Additional tier 1 capital: regulatory adjustments	
44	Additional tier 1 capital (AT1)	\$ -
45	Tier 1 Stock (T1 = CET1 + AT1)	26,777
	Tier 2 capital: regulatory adjustments	-
51	Tier 2 capital before regulatory adjustments	<u>-</u>
	Tier 2 stock before regulatory adjustments	-
59	Total Capital (TC = T1 + T2)	\$ 26,777 =====
60	Assets weighted by total risk	\$ 185,223 =====

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<u>Ref.</u>	<u>Capital Ratios and supplements</u>	<u>Amount</u>
61	Common tier 1 capital (as a percentage of the weighted assets by total risk)	14.46%
62	Tier 1 capital (as a percentage of the weighted assets by total risk)	14.46%
63	Total capital (as a percentage of the weighted assets by total risk)	14.46%
64	Institutional specific 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 risks assets)	7.46%

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2. Ratio of net capital with the balance sheet.

		Balance sheet amounts	
Balance sheet items Reference	Balance sheet items (unconsolidated)		2017
BS1	Cash and cash equivalents	\$	28,541
BS2	Margin accounts		35
BS3	Investment securities		214,800
BS4	Repurchase/resell agreements debtors		2,718
BS5	Securities lending		-
BS6	Derivatives		1,885
BS7	Valuation adjustment from hedging of financial assets		15,294
BS8	Total loan portfolio (net)		223,948
BS9	Receivable benefits on securities trading		-
BS10	Other receivables (net)		16,432
BS11	Foreclosed assets (net)		4
BS12	Premises, furniture and equipment (net)		8
BS13	Permanent investments (a)		22,641
BS14	Long-lived assets available for sale		-
BS15	Deferred income taxes and employee statutory profit sharing, net		1,861
BS16	Other assets		<u>915</u>
	Total assets	\$	<u>529,082</u> =====

(a) Includes other investments

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Balance sheets amounts		
Balance sheet items <u>reference</u>	Balance sheet items <u>unconsolidated</u>	<u>2017</u>
<u>Liabilities:</u>		
BS17	Deposit funding	\$ 259,764
BS18	Bank and other borrowings	25,401
BS19	Repurchase/resell agreement creditors	188,768
BS20	Securities lending	-
BS21	Collateral sold or furnished as a guarantee	-
BS22	Derivatives	7,785
BS23	Valuation adjustments of hedging financial liabilities	11,203
BS24	Debentures in securities trading	-
BS25	Other accounts payable	4,619
BS26	Outstanding unsecured obligations	-
BS27	Deferred income taxes and employee statutory profit sharing, net (net)	-
BS28	Deferred credits and prepayments	98
	Total liabilities	\$ 497,638
<u>Stockholders' equity:</u>		
BS29	Capital stock	\$ 23,427
BS30	Earned capital	8,017
	Total stockholders' equity	31,444
	Total liabilities and stockholders' equity	\$ 529,082

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Balance sheets amounts		
Balance sheet items reference	Balance sheet items unconsolidated	2017
<u>Memorandum Accounts:</u>		
BS31	Guarantees granted	\$ -
BS32	Contingent assets and liabilities	76,584
BS33	Loan commitments	58,606
BS34	Assets placed in trust or mandate	1,375,530
BS35	Federal Government Financial Agent	371,322
BS36	Assets in custody or administration	543,016
BS37	Collateral received by the entity	15,413
BS38	Collateral received and sold or pledged as a guarantee by the entity	12,694
BS39	Investment bank on behalf of third party	14,511
BS40	Interest earned but not collected arising from past due – loan portfolio	168
BS41	Other memorandum accounts	634,344
		634,344

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Regulatory items considered for the calculation of the net capital components.

<u>Identifier</u>	<u>Regulatory items considered for the calculation of net Capital</u>	<u>Reference to the disclosure form of the capital integration of section 1 to this exhibit</u>	<u>Amount of combination notes to regulatory concepts considered for the calculation of net capital components</u>	<u>Reference(s) of the balance sheet item and the related amount to the regulatory concepts consider for the calculation of net capital from the aforementioned reference</u>
Assets:				
15	Investments in multi-lateral agencies	26 - D	644	
17	Investment in risk capital	26 - F	3,093	
18	Investments in mutual funds	26 - G	186	
22	Investments of the defined benefits pension plan	26 - N	14,218	Informative uncomputed data
Stockholders' equity:				
34	Paid in capital in accordance with exhibit 1	1	23,427	

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<u>Identifier</u>	<u>Regulatory items considered for the calculation of net Capital</u>	<u>Reference to the disclosure form of the capital integration of section 1 to this exhibit</u>	<u>Amount of combination notes to regulatory concepts considered for the calculation of net capital components</u>	<u>Reference(s) of the balance sheet item and the related amount to the regulatory concepts consider for the calculation of net capital from the aforementioned reference</u>
35	Prior year income	2	4,148	
37	Other capital earned elements other than the foregoing	3	3,126	
41	Accumulated effect on translation	3, 26 - A	N/A	
42	Result on holding non-monetary assets	3, 26 - A	N/A	
Regulatory concepts not considered in the balance sheet:				
45	Profit or increase in the value of the assets by acquisition of securitization positions (Originating Institutions)	26 - C	N/A	
46	Transactions that contravene provisions	26 - I	N/A	
47	Relevant related parties transactions	26 - M	N/A	
48	Adjustment for capital recognition	26 - O, 41, 56	N/A	

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3. Main characteristics of the securities that are part of the net capital ("A" Series).

<u>Ref.</u>	<u>Characteristic</u>	<u>Option</u>
1	Issuer	Nacional Financiera, Sociedad Nacional de Crédito
2	Identifier ISIN, CUSIP o Bloomberg	
3	Legal framework	In conformity with Article 30 of Credit Institutions Law, Nacional Financiera, Sociedad Nacional de Crédito, Institución de Banca de Desarrollo, is governed by its internal regulations, holders of Series "A", capital contribution certificates, if applicable will have the rights set forth in article 35 of Credit Institutions Law and article 12 of internal regulations of Nacional Financiera.
<i>Regulatory treatment:</i>		
4	Capital level with transitory status	
5	Capital level without transitory status	Basic 1
6	Level of instrument	Lending institution without consolidating subsidiaries
7	Type of instrument	"A" Serie certificates of capital contribution
8	Recognized amount in regulatory capital	66% in accordance with (3)
9	Nominal value of the instrument	50.00
9A	Instrument currency	Mexican pesos
10	Book classification	Capital

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<u>Ref.</u>	<u>Characteristic</u>	<u>Option</u>
11	Issue date	
12	Instrument term	Perpetuity
13	Expiration date	Without maturity
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	
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	Instrument convertibility	Nonconvertible
24	Convertibility conditions	
25	Degree of convertibility	
26	Conversion rate	
27	Type of instrument convertibility	
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	

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4. Capital management.

The framework for risk management must facilitate and support the measurement and monitoring of quantifiable risks, ensuring solid risk measurements to establish the Institution's risk appetite and generate value.

To ensure that risk management is a decision-making support tool, models and methodologies are established, that allow for measuring, monitoring and controlling the different types of risk to which the Institution is exposed. These risk measures should also contribute to the definition of business strategies and support decision-making of operation.

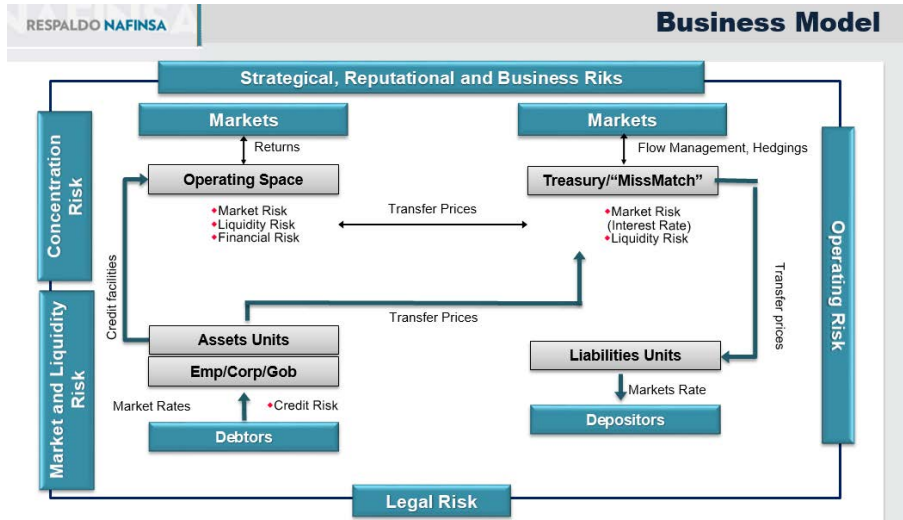
A fundamental point of departure for establishing limits is the definition of a business model that describes the exposure to different types of risk that generate the different operating units in the Institution.

- Treasury: it operates as the central unit that manages the resources of the Institution. It is responsible for establishing transfer prices, controlling liquidity levels and control the risks of balance sheet. This unit incurs risks of market, credit and liquidity risks, and in the case of the Institution is also responsible for the deposit-funding unit.
- Operation desks: their main function is to generate revenues through the operation in different financial markets, (money, foreign exchange, capital and foreign currency bonds).
- Asset units: are those that encompass the promotion activities of the Institution and are derived from credit activities. These activities are the main generators of credit risk.

(Continued)

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Based on the aforementioned, the Institution has a solid structure of global and specific limits for exposure to different types of risk considering the consolidated risk, breaking down by unit of business, factor risk and cause, as presented in the following diagram:

Capital Assignment		Capital Limits			
Limits	Markets	Market Limits	Notional Limits	VaR & Capital Limits	Operator Limit
		Credit	Particular Limits	Corporate portfolios (Issue – Issuer)	
	Credit Exposure Limit			Derivatives Limits	Agrupation Limits
	Liquidity			Institutional Limits	Prudential Limits According to Basel III
		Liquidity Indicator	Liquidity Ratio		ICAP
	Control Measures		Maximum Loss Three Times VaR		

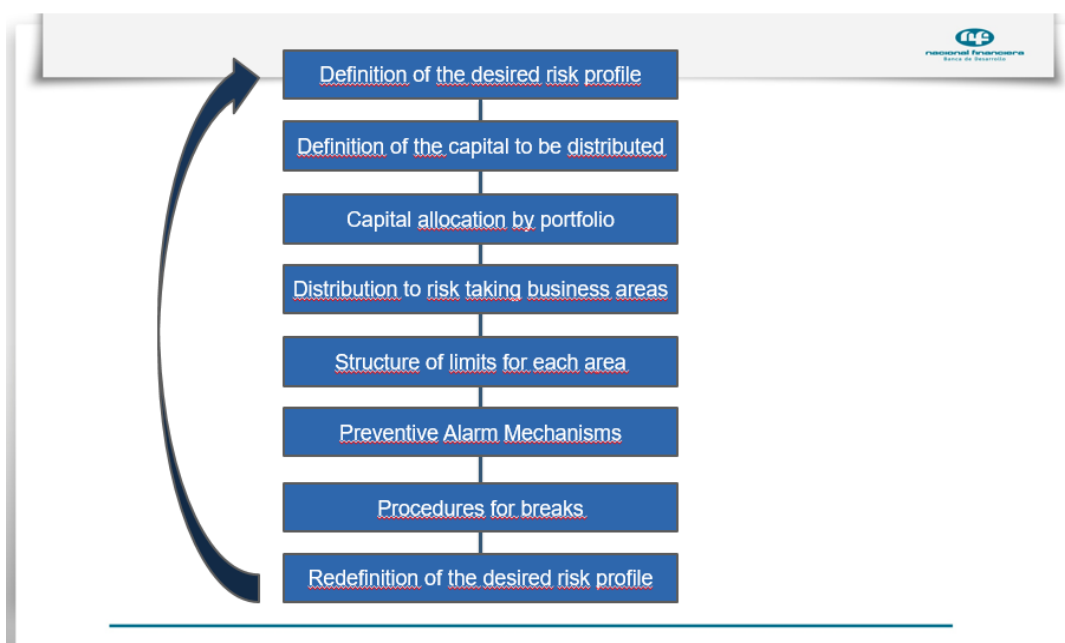
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The diagram presented in the prior page, have a strong relevance to the capital limits, for which the following process is followed to determine limits:



The capital allocation is derived from the regulatory capital, which is regulated based on capitalization rules described in annex 9 called ICAP process forms, included in the risk manual. Based on these concepts, capital distributable is determined, that is the capital that the Institution has to deal with the risks that its operations consume.

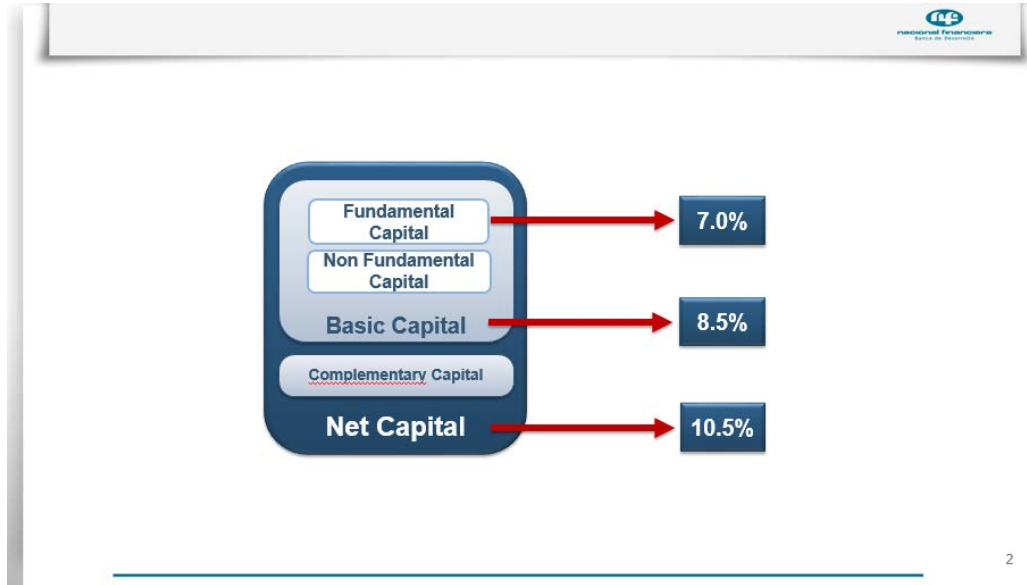
Basilea III establishes that the Institution has three indicators of solvency, where ICAP is the most restrictive, given the fact the requirement changed from 8.0% to 10.5%. It is precisely this restriction that establishes the appetite for risk through the limits of capital, in order to ensure if, 100% of consumption of the limits, and in stress situations, the level of capitalization in no case is less than 10.5%.

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This increase of 250 basis point in the ICAP is a strong regulator that will replace the capital volatility for risk profile and operational risk previously held.

Capital limits structure

The Institution's capital management considers a limits structure with two levels of allocation:

- a) A strategic level, authorized by the Board of Directors
- b) A tactical level that is regulated by the IRMC, through reallocations or excess of limits, as well as the management of the business areas.

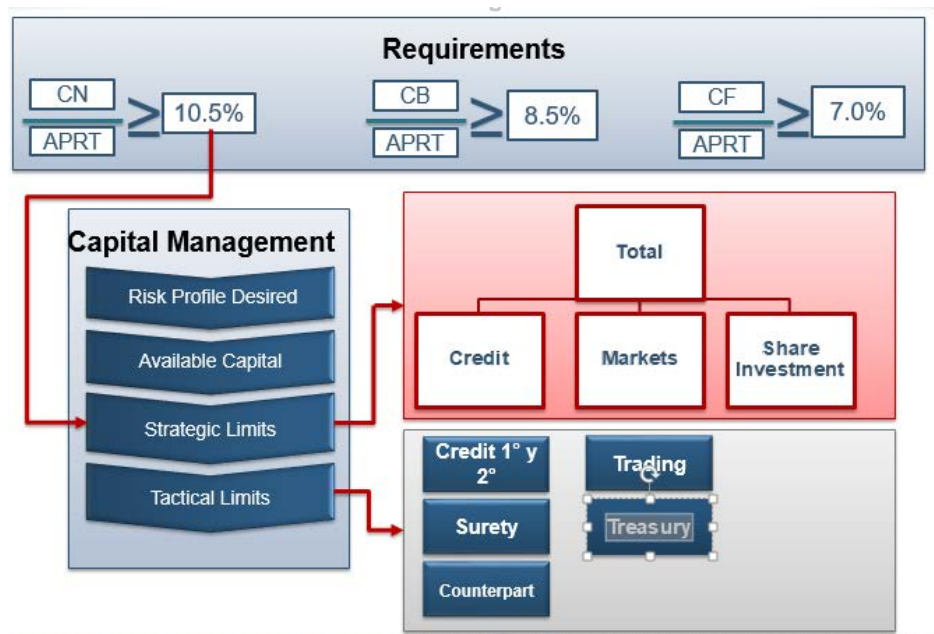
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In summary the Institution has:



Operational risk is not included within the strategic structure of these limits, given that operational risk is not originated through discretionary risk taking, this is, the own Institution's operation is implicit.

Considering the aforementioned, there is an operational risk regulator which is not computed for capital limit, however it is computed for at the capitalization level.

Notwithstanding the aforementioned, identification, measurement, supervision, control and risk mitigation, to which the Institution is exposed, are performed for operational risk.

Considering the above, at the end of December 2017, the capitalization ratio was 14.46% and the capital limit recorded a global consumption of 90.1%.

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There are three basic scenarios:

1. If capital limits are utilized at 100%, the level of funding would remain above the 10.5% required.
2. If, under the current structure, there is an adverse event of default or volatility in the markets affected by capital, there is sufficient capacity to maintain the ICAP above 10.5%
3. The combination of the above events, that is capital limits utilized at 100% and an adverse event with an impact on capital, would also allow the ICAP to be maintained above the minimum level required.

Finally, in order to have the capacity to obtain resources and continue operating under a stress scenario, in which the Institution's capital sufficiency is compromised without default of the minimums established by the authorities, the Treasury Department will obtain in the markets, the necessary resources in the best terms of cost and term, based on the guidelines established by the Institution's Management.

In order to manage liquidity risks, the treasury will regulate the operational execution in accordance with strategies that will be aligned with the Institution's Management objectives and will be responsible for detonating the contingent procedures for the management of liquidity, and in some cases, the procedures established in the "Business Continuity Plan" will apply.

The treasury department will inform to the Risk Management Officer of any liquidity contingency situation.

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(23) Memorandum accounts -

(a) Guarantees granted

At December 31, 2016, the Institution has guarantees granted for \$72, which represent a contingent risk in the event that the guaranteed debtor does not settle its debt to the credit institution. At December 31, 2017 and 2016, no losses have been recorded for guarantees in the Institution's results; however, in the event of non-compliance with any guarantee, the Institution grants a loan to fulfill its obligation.

During the year 2017 and 2016, no credits have been granted for default of any guarantee

(b) Contingent asset and liabilities

As of December 31, 2017 and 2016, this caption amounts to \$62,510 and \$53,448, respectively, integrated as follows:

		<u>2017</u>	<u>2016</u>
Contingent liabilities:			
Guarantees granted	(1) \$	72,558	63,537
Unreimbursed guarantees paid covered by counter guarantee	(2)	12,696	11,715
Receivables on claims		132	134
Acquired commitments		<u>1,888</u>	<u>2,118</u>
Subtotal carried forward	\$	<u>87,274</u>	<u>77,504</u>

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		<u>2017</u>	<u>2016</u>
Subtotal brought forward	\$	<u>87,274</u>	<u>77,504</u>
Contingent assets:			
Counter-guarantee received from the counter-guarantee trust for enterprise financing	(3)	11,340	11,645
Guarantees paid to recover covered by counter-guarantors	(4)	12,696	11,715
Guarantees paid pending of recovery without counter-guarantee	(5)	<u>728</u>	<u>696</u>
		<u>24,764</u>	<u>24,056</u>
Total	\$	<u>62,510</u>	<u>53,448</u>

(1) In this caption, the Institution has mainly guarantees granted through *Fondo para la Participación de Riesgos* and *Fondo para la Participación de Riesgos en Fianzas*, which at December 31, 2017 and 2016, both present an amount of guarantees granted for \$67,798 and \$60,116, respectively. The spread at December 31, 2017 and 2016, for \$4,760 and \$3,421, respectively, correspond to selective guarantees granted directly by the Institution. These guarantees represent the amount of the responsibilities assumed by the Institution to guarantee financial intermediaries the recovery of their loan portfolio.

(2) The Institution's contingent obligation to reimburse, mainly to the counter-guarantee Trust for Corporate Financing, the amount of the guarantees paid, has been recorded in this caption which counted with the counter-guarantee and which are in the process of recovery by bank and non-bank financial intermediaries.

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- (3) *Fondo para la Participación de Riesgos* reduces the Institution's contingency through the counter-guarantee received from *Fideicomiso de Contragarantía para el Financiamiento Empresarial*, the promoter of granting of credits for specific purposes, which has assigned resources for these purposes for \$11,340 and \$11,645, at December 31, 2017 and 2016 respectively. These funds assure, the recovery up to these amounts of the guarantees exercised by the financial intermediaries, who assume the commitment of negotiating the recovery of the credits of their final borrowers judicially and out-of-court.

In addition to this counter-guarantee, the Fund has created a preventive allowance for credit risks, for \$2,505 and \$1,175, as of December 31, 2017 and 2016 respectively, in accordance with the Provisions of the Banking Commission judicially and out-of-court.

With the counter-guarantee received, as well as with the level of preventive allowance created, the Institution considers that the exposure is covered, based on the experience observed in the guarantee program.

- (4) The contingent right of the Institution to recover the amount of the guarantees paid that had a counter-guarantee that were covered by the *Fideicomiso de Contragarantía para el Financiamiento Empresarial*, and which are in the process of recovery by bank and non-bank financial intermediaries.
- (5) In the caption of paid guarantees pending recovery without counterguarantee, is recognized the amount of guarantees honored by the Institution that are in the process of recovery by financial intermediaries and that did not have the coverage of *Fideicomiso de Contragarantía para el Financiamiento Empresarial*.

(c) Credit commitments

At December 31, 2017 and 2016, the balance of authorized credit facilities and lines of guarantees granted to financial intermediaries that have not been withdraw amounted \$172,948 and \$135,025, respectively. At December 31, 2017, \$58,606 correspond to credit and \$ 114,342 to lines guarantee granted, respectively, where as at December 31, 2016, \$44,013 correspond to lines of credit and \$91,012 to lines of guarantees granted, respectively.

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(d) Assets placed in trust or mandates

The Institution's trust activity recorded in memorandum accounts as of December 31, 2017 and 2016, as well as operations as financial agent for the federal Government, are integrated as shown below:

	<u>2017</u>	<u>2016</u>
Investments trusts	\$ 14,619	25,967
Administrative trusts	1,311,276	1,093,806
Guarantee trusts	<u>13,823</u>	<u>46,685</u>
	1,399,718	1,166,458
Mandates	<u>14,133</u>	<u>13,716</u>
	1,353,851	1,180,174
Financial Agent of the Federal Government	<u>371,322</u>	<u>364,371</u>
Total	\$ <u>1,725,173</u>	<u>1,544,545</u>

Investment and administrative trusts refer to entities with their own legal incorporation, 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 trustee.

Guarantee trusts correspond to entities that maintain loans, securities, real estate, etc., as part of its trust assets, which serve as collateral for the settlement of financing received from other credit institutions by the trustees of the same. The Institution only performs the fiduciary function in such entities.

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The Institution's revenue from its trustee activities at December 31, 2017 and 2016, amounted to \$184 and \$189, respectively.

As of December 31, 2017 and 2016, the trust accounts include a balance of \$ 398 and \$ 449, respectively, which corresponds to the assets of *Fideicomiso de Recuperación de Cartera (FIDERCA)*, which manages doubtful accounts that were originally of the Institution and that in the year of 1996 were transferred to the Federal Government. The Institution currently holds the respective trustee rights.

1. The Institution incorporated the trust for the strengthening of its capital in compliance with the provisions of article 55 Bis of Credit Institution Law and in accordance with the general rules for Domestic Lending Institutions and Development Banking Institutions published on October 24, 2002 in Official Federal Gazette.

(e) Assets in custody or administration-

As of December 31, 2017 and 2016, this caption includes, trading securities and credit operations, as well as the securities issued by the Institution and managed on behalf of clients, as shown below

	<u>2017</u>	<u>2016</u>
Custody	\$ 15,676	70,324
Pledge securities	245,636	235,720
Collection	-	1
Securities in administration	281,704	275,309
Subsidiaries	<u>13,653</u>	<u>12,151</u>
	<u>\$ 556,669</u>	<u>593,505</u>

Fees collected by the Institution for this type of activities for the years ended December 31, 2017 and 2016, amounted to \$8 in both years.

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(f) Other memorandum accounts -

As of December 31, 2017 and 2016, the balances of other memorandum accounts are comprised as follows:

		<u>2017</u>	<u>2016</u>
Guarantees paid reported by brokers as uncollectible without a counterguaranty	(a)	\$ 170	71
Classification by degree of risk of the credit portfolio		302,405	277,922
Loans obtained pending for disbursements (note18)		2,657	3,005
Other memorandum accounts	(b)	<u>336,458</u>	<u>329,809</u>
Total		\$ <u>641,690</u>	<u>610,807</u>

- (a)** Correspond to the amounts of unrecovered guarantees on which the collection procedures have been concluded by the intermediaries and which did not have a counterguarantee.
- (b)** Other memorandum accounts are included for control of renewed and restructured loans, uncollectible credits, uncollectible loans applied against the provision, mortgage-backed loans, certificates and coupons to be incinerated, VAT recorded by states, portfolio recovery, issue of provisional certificates, foreclosed assets written-off preventively, control of amounts contracted in repurchase/resell agreements and derivative instruments, commitments, allowance for loan losses from financial brokers and various unspecified items.

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(24) Additional information on operations and segments-

(a) Segment information (not audited) -

The factors used to identify the 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 monitoring regularly performed on the results generated that are presented regularly to the Board of Directors of the Institution.

The market and treasury segment includes investments carried out in the money, capital, exchange and treasury markets.

The loan portfolio placed directly with the public and private sector, is considered for the first tier credit segment while the loan portfolio channeled through banking and non-banking financial intermediaries is considered for the second tier credit.

Guarantees granted to banks and non-bank financial intermediaries are included in the credit guarantees segment. The balances of this segment are presented in memorandum accounts and as of December 31, 2017 and 2016, amount to \$66,147 and \$59,594, respectively.

The balances of the Financial Agent segment correspond to activities carried out by mandate of the Federal Government, to manage on its behalf, resources obtained from international financial organizations, and as of December 31, 2017 and 2016, amounted to \$371,387 and \$364,465, respectively, of which \$371,322 and \$364,371, respectively, are recorded in memorandum accounts.

The trustee segment includes administrative services for own an external trusts, which amount to \$1,361,397 and \$1,166,458, respectively as of December 31, 2017 and 2016.

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Investment banking and balances of Subsidiaries are included in the “other areas segment”. Commissions for structuring of credits, stock market guarantees, as well as the participation in venture capital for public and private companies are included in investment banking.

As of December 31, 2017 and 2016, the assets, liabilities and net income of the main operations by business segments of the Institution are presented below

2017

<u>Business segment</u>	<u>Assets</u>		<u>Liabilities & Equity</u>		<u>Net income</u>	
	<u>Amount</u>	<u>%</u>	<u>Amount</u>	<u>%</u>	<u>Amount</u>	<u>%</u>
Markets and treasury	\$ 271,584	52.6	271,584	52.6	1,269	84.5
First tier credit	63,004	12.2	63,004	12.2	630	41.9
Second tier credit	165,390	32.0	165,390	32.0	395	26.3
Loan guarantees	-	-	-	-	564	37.5
Financial agent	65	-	65	-	80	5.4
Trustee	-	-	-	-	(27)	(1.8)
Other areas	16,187	3.2	16,187	3.2	111	7.3
Retirement benefit and expense	-	-	-	-	(1,520)	(101.1)
Total	\$ 516,230	100	516,230	100	1,502	100

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2016

<u>Business Segment</u>	<u>Assets</u>		<u>Liabilities & Equity</u>		<u>Net income</u>	
	<u>Amount</u>	<u>%</u>	<u>Amount</u>	<u>%</u>	<u>Amount</u>	<u>%</u>
Markets and treasury	\$ 262,631	52.10	262,632	52.10	1,168	86.33
First tier credit	66,299	13.16	66,299	13.16	(125)	(9.24)
Second tier credit	147,920	29.36	147,920	29.36	809	59.79
Loan guarantees	-	-	-	-	842	62.23
Financial agent	94	0.02	94	0.02	101	7.46
Trustee	-	-	-	-	(8)	(0.59)
Other areas	26,846	5.36	26,845	5.36	302	22.32
Retirement benefit and expense	-	-	-	-	(1,736)	(128.30)
Total	\$ 503,790	100	503,790	100	1,353	100

For the years ended December 31, 2017 and 2016, income by segment is analyzed in the next page.

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	<u>Markets and Treasury</u>	<u>First tier credit</u>	<u>Second tier credit</u>	<u>Loan Guarantees</u>	<u>Financial agent</u>	<u>Trustee</u>	<u>(a) other areas</u>	<u>Retirement benefit and expense</u>	<u>Total</u>	
2017										
<i>Income:</i>										
Financial income net	\$ (a)	1,851	873	1,416	2,632	225	192	266	-	7,455
<i>Expenses:</i>										
Operating expense		<u>(361)</u>	<u>(77)</u>	<u>(656)</u>	<u>(340)</u>	<u>(130)</u>	<u>(201)</u>	<u>(149)</u>	<u>-</u>	<u>(1,914)</u>
Operating income		1,490	796	760	2,292	95	(9)	117	-	5,541
Allowance for loan losses and write-offs		(4)	(58)	(301)	(1,603)	(2)	(3)	(1)	-	(1,972)
Retiree expense		-	-	-	-	-	-	-	(970)	(970)
Other expenses and taxes	(b)	<u>(217)</u>	<u>(108)</u>	<u>(64)</u>	<u>(125)</u>	<u>(13)</u>	<u>(15)</u>	<u>(5)</u>	<u>(550)</u>	<u>(1,097)</u>
Net income	\$	<u>1,269</u>	<u>630</u>	<u>395</u>	<u>564</u>	<u>80</u>	<u>(27)</u>	<u>111</u>	<u>(1,520)</u>	<u>1,502</u>
2016										
<i>Income</i>										
Financial income net	\$	1,613	552	1,390	2,248	233	193	401	-	6,630
<i>Expenses:</i>										
Operating expense		<u>(350)</u>	<u>(72)</u>	<u>(640)</u>	<u>(332)</u>	<u>(121)</u>	<u>(188)</u>	<u>(109)</u>	<u>-</u>	<u>(1,812)</u>
Operating income		1,263	480	750	1,916	112	5	292	-	4,818
Allowance for loan losses and write-offs		(4)	(601)	115	(633)	(2)	(3)	(1)	-	(1,129)
Retiree expense		-	-	-	-	-	-	-	(936)	(936)
Other expenses and taxes	(c)	<u>(91)</u>	<u>(4)</u>	<u>(56)</u>	<u>(441)</u>	<u>(9)</u>	<u>(10)</u>	<u>11</u>	<u>(800)</u>	<u>(1,400)</u>
Net income	\$	<u>1,168</u>	<u>(125)</u>	<u>809</u>	<u>842</u>	<u>101</u>	<u>(8)</u>	<u>302</u>	<u>(1,736)</u>	<u>1,353</u>

(a) Includes the following areas: investment banking, subsidiaries and other income (expenses) net.

(b) Includes \$547 of taxes and ESPS current and deferred.

(c) Includes \$632 of taxes and ESPS current and deferred.

(Continued)

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During 2017, accumulated earnings for the segment markets and treasury amounted to \$1,851, comprised of \$1,611 generated by the operation of different markets and treasury, which was higher by 5.8% in relation to 2016.

As of December 31, 2017, the net income for the First tier credit amounted to \$873, comprised of \$528 of financial margin; other net income by \$314 associated with structuring commissions, as well as \$31 of other commissions.

The accumulated financial income for the year ended December 31, 2017 for the Second tier credit amounted to \$1,416, of which \$1,327 correspond to financial margin and \$89 to commissions and other net income associated with the credit operation. The amount of net financial income in 2017 was 1.8% higher than 2016, due to the reduction of 11 basis points in the weighted margin of the loan portfolio. This reduction in the financial margin was consistent with the institutional strategy of offering more competitive rates to intermediaries. Likewise, the average balance between both periods increased from, \$122,080 in 2016 to \$138,514 in 2017 (13.5%), in line with the institutional strategy.

At December 31, 2017, in the credit guarantees segment increases net financial income of \$2,632, (\$1,737 of fees charged for the guarantees granted, as well as \$ 895 of interest on investments and net recoveries).

The net financial income of the credit guarantees segment includes 17.1%, from 2016 to 2017, mainly due to the growth in the balance of own guarantees granted during the last twelve months, increasing from \$63,536 to \$ 72,558.

As of December 31, 2017, the net financial income of the Financial Agent segment amounted to \$225, increasing the balance related to mandates in dollars by 6.2%.

During 2017, in the Trustee segment, non-financial income was collected for \$192, slightly lower than obtained in the prior year.

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(b) Financial margin

For the years ended December 31, 2017 and 2016, the financial margin in the consolidated statement of income is comprised as follows:

	2017		
	Total	Local Currency	Foreign Currency
<i>Interest income:</i>			
Interests of performing loan portfolio:			
Commercial loans	\$ 2,577	1,038	1,539
Mortgage loans	4	4	-
Consumer loans	1	1	-
Loans to government entities	1,085	1,085	-
Credits granted as agent of The Federal Government	2	-	2
Loans to financial entities	<u>10,189</u>	<u>9,913</u>	<u>276</u>
	<u>13,858</u>	<u>12,041</u>	<u>1,817</u>
Interests and returns earned on investments in securities			
- Trading securities	1,481	1,481	-
- Securities available for sale	297	-	297
- Securities held to maturity	<u>1,168</u>	<u>1,124</u>	<u>44</u>
	<u>2,946</u>	<u>2,605</u>	<u>341</u>
Interests and returns earned on repurchase / resell agreements:	<u>15,286</u>	<u>15,286</u>	<u>-</u>
Cash and cash equivalents interest:			
Banks	214	-	214
Restricted cash and cash equivalents	<u>1,031</u>	<u>979</u>	<u>52</u>
	<u>1,245</u>	<u>979</u>	<u>266</u>
Subtotal carried forward	\$ <u>33,335</u>	<u>30,911</u>	<u>2,424</u>

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		<u>2017</u>	
	<u>Total</u>	<u>Local currency</u>	<u>Foreign currency</u>
Subtotal brought forward	\$ 33,335	30,911	2,424
Commissions from credit operations:			
Commercial loans	79	79	-
Interest and returns from margin accounts	6	-	-
Revenues from hedging transactions	(7)	134	(141)
Premium on debt placement	12	12	-
Equity dividends	<u>49</u>	<u>49</u>	<u>-</u>
	<u>139</u>	<u>280</u>	<u>(141)</u>
Total interest income	<u>33,474</u>	<u>31,191</u>	<u>2,283</u>
<i>Interest expenses:</i>			
Interest from time deposits	8,136	7,738	398
Interest on securities issued	4,435	3,590	845
Interest charged on interbank loans and other agencies	491	246	245
Interests and returns on to repurchase / resell agreements	14,781	14,781	-
Expenses from hedge trading	(701)	(3,413)	2,712
Discounts for debt issued	34	34	-
Issuance expenses due to debt placement	18	7	11
Loss from valuation	<u>1,015</u>	<u>-</u>	<u>1,015</u>
Total interest expenses	<u>28,209</u>	<u>22,983</u>	<u>5,226</u>
Financial margin	\$ 5,265	8,208	(2,943)

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(Millions of Mexican pesos)

	2016		
	<u>Total</u>	<u>Local currency</u>	<u>Foreign currency</u>
<i>Interest income:</i>			
Interests of performing loan portfolio			
Commercial loans	\$ 2,114	898	1,216
Mortgage loans	2	2	-
Loans to government entities	716	715	1
Credits granted as agent of the Federal Government	3	-	3
Loans to financial entities	<u>6,014</u>	<u>5,738</u>	<u>276</u>
	<u>8,849</u>	<u>7,353</u>	<u>1,496</u>
Interests and returns earned on:			
- Trading securities	714	714	-
- Securities available for sale	278	-	278
- Securities held to maturity	<u>733</u>	<u>684</u>	<u>49</u>
	<u>1,725</u>	<u>1,398</u>	<u>327</u>
Interests and returns earned on repurchase / resell agreements:	<u>10,097</u>	<u>10,097</u>	<u>-</u>
Cash and cash equivalents interest:			
Banks	46	-	46
Restricted cash and cash equivalents	<u>656</u>	<u>637</u>	<u>19</u>
	<u>702</u>	<u>637</u>	<u>65</u>
Subtotal carried forward	\$ <u>21,373</u>	<u>19,485</u>	<u>1,888</u>

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(Millions of Mexican pesos)

	2016		
	<u>Total</u>	<u>Local currency</u>	<u>Foreign currency</u>
Subtotal brought forward	\$ <u>21,373</u>	<u>19,485</u>	<u>1,888</u>
Commissions from credit operations:			
Commercial loans	94	94	-
Revenues from hedging transactions	(425)	(166)	(259)
Premium on debt placement	13	13	-
Gain on currency translation	127	-	127
Equity dividends	<u>9</u>	<u>9</u>	<u>-</u>
	<u>(182)</u>	<u>(50)</u>	<u>(132)</u>
Total interest income	<u>21,191</u>	<u>19,435</u>	<u>1,756</u>
<i>Interest expenses:</i>			
Interest from time deposits	4,987	4,823	164
Interest on securities issued	3,214	2,687	527
Interest charged on interbank loans and other agencies	469	235	234
Interests and returns on charged to repurchase / resell agreements	9,057	9,057	-
Expenses from hedge trading	<u>(1,277)</u>	<u>(2,863)</u>	<u>1,586</u>
Total interests expenses	<u>16,450</u>	<u>13,939</u>	<u>2,511</u>
Financial margin	\$ <u>4,741</u>	<u>5,496</u>	<u>(755)</u>

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(Millions of Mexican pesos)

(c) Commission and fee income -

For the years ended December 31, 2017 and 2016, the commissions and fee income are analyzed as follows:

	2017		
	Total	Local currency	Foreign currency
<i>Commissions and fees earned:</i>			
Guarantees	\$ 1,848	1,848	-
Credit operations	347	347	-
Guarantees granted	1	1	-
Assets in custody or administration	8	8	-
Trustee activities	330	330	-
Others	<u>291</u>	<u>209</u>	<u>82</u>
	\$ <u>2,825</u>	<u>2,743</u>	<u>82</u>
<i>Commissions and fees paid:</i>			
Loans received	\$ 11	-	11
Debt placement	3	2	1
Distribution	107	107	-
Others (services)	<u>110</u>	<u>106</u>	<u>4</u>
	\$ <u>231</u>	<u>215</u>	<u>16</u>

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	2016		
	<u>Total</u>	<u>Local Currency</u>	<u>Foreign Currency</u>
<i>Commissions and fees paid earned:</i>			
Guarantees	\$ 1,931	1,931	-
Credit operations	195	195	-
Guarantees granted	2	2	-
Assets in custody or administration	8	8	-
Trustee activities	334	334	-
Others	<u>301</u>	<u>230</u>	<u>71</u>
	\$ <u>2,771</u>	<u>2,700</u>	<u>71</u>
<i>Commissions and fees paid:</i>			
Loans received	\$ 24	-	24
Debt placement	9	9	-
Distribution	142	142	-
Others (services)	<u>114</u>	<u>108</u>	<u>6</u>
	\$ <u>289</u>	<u>259</u>	<u>30</u>

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(d) Financial intermediation income-

For the years ended December 31, 2017 and 2016, financial intermediation income is analyzed as follows:

		<u>2017</u>	
	<u>Total</u>	<u>Local currency</u>	<u>Foreign currency</u>
Valuation result at fair value and decrease for securities valued at cost:			
Trading securities	\$ 167	167	-
Derivative financial instruments for trading purposes	206	(40)	246
Derivative financial instruments for hedging purposes	34	(36)	70
Collaterals sold	<u>(1)</u>	<u>(1)</u>	<u>-</u>
	<u>406</u>	<u>90</u>	<u>316</u>
Realized gain or (loss)			
Trading securities	146	146	-
Securities available for sale	(19)	-	(19)
Derivate financial instruments for trading purposes	<u>1,173</u>	<u>1,173</u>	<u>-</u>
	<u>1,300</u>	<u>1,319</u>	<u>(19)</u>
Result on trading currency	<u>(2,914)</u>	<u>-</u>	<u>(2,914)</u>
Financial intermediation income	\$ <u><u>(1,208)</u></u>	<u><u>1,409</u></u>	<u><u>(2,617)</u></u>

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	2016		
	<u>Total</u>	<u>Local currency</u>	<u>Foreign currency</u>
Valuation result at fair value and decrease for 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)
Collaterals sold	<u>(301)</u>	<u>(301)</u>	<u>-</u>
	<u>10</u>	<u>1,506</u>	<u>(1,496)</u>
Realized gain or (loss)			
Trading securities	565	565	-
Securities held to maturity	2	-	2
Securities available for sale	(26)	-	(26)
Derivatives financial instruments for trading purpose	<u>3,804</u>	<u>3,804</u>	<u>-</u>
	<u>4,345</u>	<u>4,369</u>	<u>(24)</u>
Result on trading currency	<u>(5,101)</u>	<u>-</u>	<u>(5,101)</u>
Financial intermediation income:	\$ <u>(746)</u>	<u>5,875</u>	<u>(6,621)</u>

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(e) Other operation income (expenses)-

For the years ended December 31, 2017 and 2016, other operating income (expenses) is analyzed as follows:

	<u>2017</u>		
	<u>Total</u>	<u>Local currency</u>	<u>Foreign currency</u>
<i>Other operating income (expenses):</i>			
Reversal of excesses from			
allowance for loan losses	\$ 930	776	155
Other recoveries	46	46	-
Estimation due to irrecoverability or difficult collection	(190)	(190)	-
Allowance for irrecoverability foreclosed assets	(5)	(5)	-
Other losses	(16)	(16)	-
Income on sale of foreclosed assets	2	2	-
Income on loans to employees	41	41	-
Other items of income (expenses) of the operation	(a) 228	226	1
Lease income	<u>57</u>	<u>57</u>	<u>-</u>
	\$ 1,093	937	156
	<u>=====</u>	<u>====</u>	<u>====</u>

(a) On December 13, 2017, the Institution paid \$550, in accordance with official letter number 102-B-057 dated December 11, 2017, issued by Ministry of Finance and Public Credit, whereby Federal Government instructs the Institution to pay based on the legal nature of use for furnishing sovereign guarantee of the Federal Government.

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	<u>2016</u>		
	<u>Total</u>	<u>Local currency</u>	<u>Foreign currency</u>
<i>Other operating income (expenses):</i>			
Reversal of excesses from allowance for loan losses	\$ 579	426	153
Allowance for irrecoverability	(157)	(157)	-
Allowance for foreclosed assets	(3)	(3)	-
Other losses	(7)	(7)	-
Income on sale of foreclosed assets	2	2	-
Income on loans to employees	40	40	-
Other items of income (expenses) of the operation	(b) (382)	(382)	-
Other recoveries	13	13	-
Lease income	<u>52</u>	<u>52</u>	<u>-</u>
	\$ <u>137</u>	<u>(16)</u>	<u>153</u>

(b) On December 9, 2016, the Institution paid \$800, in accordance with official letter number 102-B-023 dated December 8, 2016, issued by *Ministry of Finance and Public Credit*, whereby the Federal Government instructs the Institution to pay based on the legal nature of use for furnishing a sovereign guarantee of the Federal Government.

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(f) Financial ratios (not audited) -

The following are the main quarterly financial ratios of the Institution, as of and for the years ended December 31, 2017 and 2016

	2017			
	<u>1st Q</u>	<u>2nd Q</u>	<u>3rd Q</u>	<u>4th Q</u>
Delinquency index	1.06%	0.92%	0.88%	0.82%
Coverage of past due loan portfolio index.	273.82%	319.81%	333.85%	375.81%
Operating efficiency (administrative and promotional expenses / average total assets)	0.72%	0.68%	0.68%	0.59%
ROE (annualized net income for the quarter/ average stockholder's equity)	1.64%	3.73%	5.65%	4.57%
ROA (annualized net income for the quarter / average total assets)	0.10%	0.24%	0.33%	0.29%
Net capital/ Assets at credit risk	21.74%	22.08%	21.11%	21.78%
Net capital/ Assets at credit, market and operational risk.	13.32%	13.84%	13.41%	14.46%
Liquidity (liquid assets / liquid liabilities)	497.83%	853.86%	4,459.17%	406.49%
Financial margin after allowance for loan losses/ average earning assets	0.67%	0.62%	0.34%	0.61%

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	2016			
	<u>1st Q</u>	<u>2nd Q</u>	<u>3rd Q</u>	<u>4th Q</u>
Defaulting index	0.94%	1.21%	1.11%	1.02%
Coverage of past due loan portfolio index	291.79%	222.51%	232.54%	258.90%
Operating efficiency (administrative and promotional expenses / average total assets)	0.81%	0.85%	0.67%	0.54%
ROE (annualized net income for the quarter/ average stockholder's equity)	11.73%	4.62%	7.06%	(3.03%)
ROA (annualized net income for the quarter / total average assets)	0.78%	0.29%	0.39%	(0.17%)
Net capital/ Assets at credit risk	23.33%	23.32%	20.94%	19.60%
Net capital/ Assets at credit, market and operational risk.	13.88%	14.52%	13.31%	13.26%
Liquidity (liquid assets / liquid liabilities)	273.57%	962.77%	436.54%	278.63%
Financial margin after allowance for loan losses/ average earning assets	0.92%	0.63%	0.79%	0.67%

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(25) Commitments and contingencies-

(a) Leases-

Leases provide periodic rental adjustments expense, based on changes in various economic factors. Total rental expense in office property, software and others for the years ended December 31, 2017 and 2016, amounted to \$96 and \$86, respectively.

(b) Claims and trials -

In the normal course of operations, the Institution is involved in some claims and trial, which are not expected to have a material adverse effect on the financial situation and results of its operations. In such cases that represent a probable loss or make a cash outflow, the Institution has made necessary provisions.

(c) Labor liabilities-

There is a contingent liability derived from employee's benefits, which are mentioned in note 3s.

(26) Risk management (not audited information)-

The national and international regulations on risk management have seen an unprecedented evolution in recent years, incorporating a preventive approach in the financial processes carried out by credit institutions, as well as the obligation to issue internal guidelines to establish controls in order to foresee any economic loss due to the materialization of risks, whether discretionary, non-discretionary or even non-quantifiable.

The Institution, at the same time implement the requested by the various provisions of prudential nature in matters of risk management, credit and internal control, applicable to credit institutions, as well as what is indicated by regulatory bodies in Mexico on prevention of money laundering, has tried to implement international standards from a systematic and integral perspective within its controls and processes.

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Discretionary quantifiable risks

Risk of market-

The Institution uses the VaR methodology to calculate the market risk of its trading portfolios and available for sale. In general, the methodology that is being applied is the historical simulation. As general principles, the following stand out:

- The confidence interval that is being applied in the VaR calculation is 97.5% (considering the extreme left of the profit and loss distribution).
- The base time horizon considered is 1 day.

In the generation of scenarios, a year of historical information is considered in the risk factors and the risk factors related to domestic and foreign interest rates, spreads, exchange rates, indices and share prices are considered. In addition to the VaR information, sensitivity measures are calculated and stress tests are carried out ("stress-test").

As of July 2005, backtesting tests are carried out on a monthly basis to statistically validate that the market risk measurement model provides reliable results within the parameters chosen by the Institution. As of December 31, 2017, the limits to which they are monitored on a daily basis are:

- I. Value at risk: certain based on the capital allocated to market risks.

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- II. Regulatory capital: based on the rules for the capitalization requirements of the *Instituciones de Banca Multiple* and *Sociedades Nacionales de Crédito* and *Instituciones de Banca de desarrollo*.
- III. Nocionales: referring to the maximum nominal values that can be held in position.
- IV. Maximum loss measure: a limit of maximum losses is established in the face of unfavorable market trends.

The amount of the average VaR for the year 2017 is \$ 101,028, which represents 0.38% of the net capital at the end of December 2017.

Markets	
Amount VaR \$101.028 MDP	
Trading	Treasury
VaR \$70.984 MDP	VaR \$30.044 MDP

Management of assets and liabilities-

The management of assets and liabilities refers to the management of risks that affect the Institution's balance sheet. It includes the management techniques and tools necessary to identify, measure, monitor, control and manage the financial risks (liquidity and interest rates) to which the balance sheet is exposed, and also aims to maximize its adjusted performance due to market risks and, consequently, optimize the use of the Institution's capital.

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**Nacional Financiera, S. N. C.,
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Liquidity risk-

The liquidity risk that affects a banking institution is classified broadly into three categories:

- I. Market liquidity risk: is the possibility of economic loss due to the difficulty of alienating or cover assets without a significant reduction in its price. This kind of risk as a result of drastic interest rate movements, are incurred when taken in large positions in any instruments or investments are made in markets or instruments for which there is a wide supply and demand in the market.
- II. Funding liquidity risk: represents the difficulty of an institution to obtain the necessary results and settle their liabilities, through revenue, which is their assets or through the acquisition of new liabilities. This kind of crisis is usually caused by a sudden and drastic deterioration in the quality of assets that originates an extremely difficult to turn them into liquid resources.
- III. Liquidity risk by mismatch in cash flows: the inability to meet the present and future needs of cash flows affecting daily operations or financial conditions of the institution, as well as the potential loss by the change in the structure of the balance sheet of the institution because of the time difference between assets and liabilities.

The institution, in compliance with the provisions of comprehensive risk management, developed a contingency financing Plan and stages of stress liquidity, laying down various measures to monitor, quantify and follow up to the risks listed above, as well as a plan of action at the institutional level, with possible liquidity problems.

Expiry profile in local currency-

Active and passive operations in national currency increased 1% during the year 2017 compared to the previous year, standing at the end of December at \$ 472,803. Based on regulatory criteria, the maturity gap considers both balance sheet items and memorandum accounts, that is, repo and derivatives. It should be noted that the national currency to be delivered for the sale of dollar forwards has been reclassified as a liability, as the valuation of cross-currency swaps has been reclassified to the asset.

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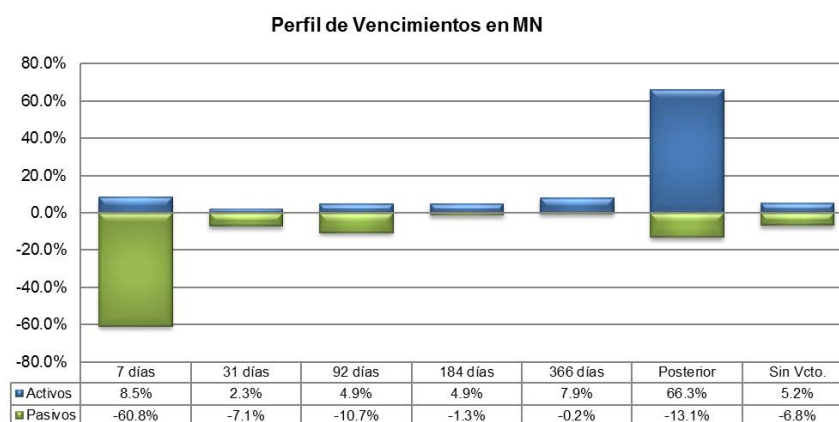
Nacional Financiera, S. N. C.,
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Maturity Ranges	2017			2016		
	Assets	Liabilities	Gap	Assets	Liabilities	Gap
Up to 7 days	\$ 40,189	287,435	(247,246)	31,084	310,287	(279,203)
Up to 31 days	10,885	33,711	(22,826)	14,357	45,647	(31,290)
Up to 92 days	23,208	50,775	(27,567)	26,096	31,106	(5,010)
Up to 184 days	23,377	6,272	17,105	18,714	3,630	15,084
Up to 366 days	37,241	985	36,256	29,647	403	29,244
Subsequent	313,454	62,171	251,283	325,430	50,420	275,010
With no defined maturity	<u>24,449</u>	<u>31,454</u>	<u>(7,005)</u>	<u>22,874</u>	<u>26,709</u>	<u>(3,835)</u>
Total	\$ <u>472,803</u>	<u>472,803</u>	<u>-</u>	<u>468,202</u>	<u>468,202</u>	<u>-</u>

The gap of negative liquidity on the horizon of a month amounts to \$270,072, \$(40,421) less than the level recorded in 2016 which amounted to \$310,493.



Expiry profile in foreign currency

Active and passive operations in foreign currency as of December 31, 2017 increased by 17.7% during the year, in relation to the year 2016, resulting from a greater amount in assets and liabilities of less than three months. Based on regulatory criteria, the maturity gap considers both balance sheet items and memorandum accounts, that is, repurchase agreements and derivatives.

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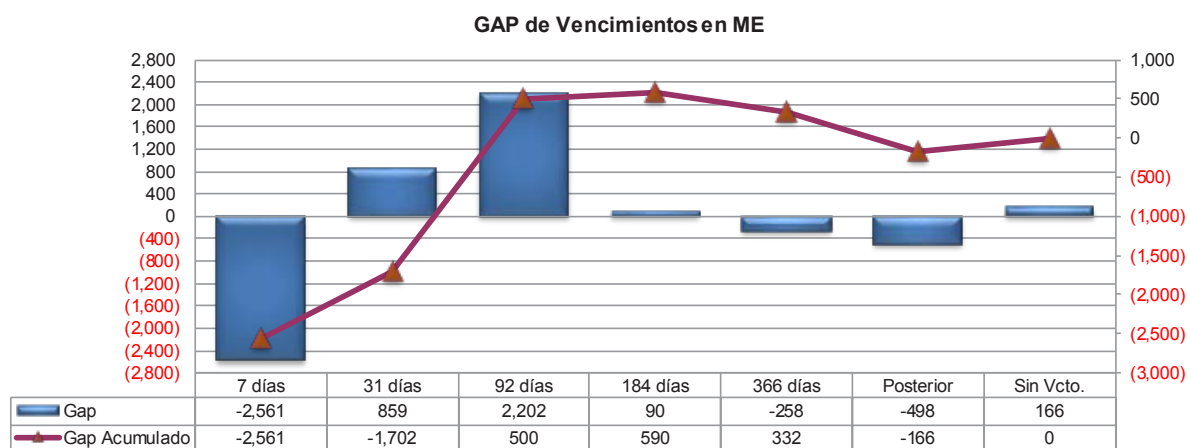
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Maturity Ranges	2017			2016		
	Assets	Liabilities	Gap	Assets	Liabilities	Gap
Up to 7 days	\$ 853	3,414	(2,561)	1,690	2,590	(900)
Up to 31 days	1,772	913	859	1,213	574	639
Up to 92 days	2,855	653	2,202	1,193	1,031	162
Up to 184 days	316	226	90	79	235	(156)
Up to 366 days	54	312	(258)	471	131	340
Subsequent	2,010	2,508	(498)	2,009	2,256	(247)
With no defined maturity	<u>166</u>	<u>-</u>	<u>166</u>	<u>162</u>	<u>-</u>	<u>162</u>
Total	\$ <u>8,026</u>	<u>8,026</u>	<u>-</u>	<u>6,817</u>	<u>6,817</u>	<u>-</u>

In accordance with the contractual maturity of assets and liabilities in foreign currency and based on figures of the balance sheet at the end of December 2017, can be seen that there was a negative \$2,561 million dollar liquidity in the first 7 days of January of 2017.



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Estimate of gain or loss on advance sale.

To comply with the provisions of article 81 of the section I, subparagraph (b)), provisions, below, is the estimation of results by advance sales of assets under normal and extreme scenarios.

At the end of December 2017, considering the scenarios of crisis in the portfolios of corporate trading and investment to maturity, if there is a similar situation to October 16, 2008, would lead to a loss of \$150.40, equivalent to the 0.93% of the value of the position.

Portfolio MN	Position	Advance Sale	Crisis scenarios					
			21/12/94	25/08/98	11/09/01	19/09/02	28/04/04	16/10/08
Corporate trading	\$ 4,587.58	0.17	-1.01	1.91	2.58	0.72	0.76	0.17
Investment to maturity	\$ 11,636.29	-137.60	-93.84	-123.33	-3.07	-22.99	-137.60	-150.57

Considering the crisis scenarios on the portfolios available for sale of the branch of Grand Cayman and investment at maturity of the London branch and Grand Cayman, there is a situation similar to the 2008 crisis could result in a loss of \$72.76 equals the 0.87% of the value of the position.

Portfolio MN	Position	Advance Sale	Crisis scenarios					
			21/12/94	25/08/98	11/09/01	19/09/02	28/04/04	16/10/08
Available for sale	6,989.20	-199.21	-18.43	-199.21	-234.05	-92.65	-77.17	-61.02
Held to maturity.	1,398.99	-21.70	-5.40	-49.33	-5.29	-21.70	-18.48	-11.74

Credit risk-

Credit risk is defined as the possibility that a counterparty or accredited breach in time and form with their credit obligations, also refers to the loss of value of investment determined by the change in the credit quality of some counterpart or credited, without that necessarily occurs a default.

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Expected loss-

The expected loss of the loan portfolio is obtained using the portfolio rating methodology established in Chapter V of the Provisions, regarding the rating of the loan portfolio. Considering this methodology, the following assumptions are also established:

- The portfolio of former employees is excluded, in order to directly measure the effect of the expected losses of the portfolio with risk from the private sector.
- The contingent portfolio of the credit to the Trust for the Participation of Risks is not considered since this trust is in charge of managing its credit risk.
- Additional reserves are not included.
- The financial agent portfolio is not considered as it is a portfolio without risk
- The nonperforming portfolio is considered, since according to the portfolio qualification methodology based on expected loss, when an event of default occurs, it does not imply that the expected loss is reserved at 100%.

Under the aforementioned assumptions, at the end of December 2017, the total portfolio stood at \$ 228,263, while the expected loss from the loan portfolio amounted to \$ 2,729.3 equivalent to 1.20% of the rated portfolio and 1.19% of the total portfolio.

<u>Portfolio</u>	<u>Expected losses allowance</u>		
	<u>Portfolio balance</u>	<u>Expected loss</u>	<u>% Expected loss</u>
Excepted	\$ 134.5	-	0.00%
Risk A	191,168.0	1,511.4	0.79%
Risk B	34,678.7	750.0	2.16%
Risk C	321.4	23.9	7.42%
Risk D	235.4	105.9	45.00%
Risk E	<u>1,859.2</u>	<u>338.1</u>	<u>18.19%</u>
Rated	<u>228,263.0</u>	<u>2,729.3</u>	<u>1.20%</u>
Total	\$ <u>228,397.5</u>	<u>2,729.3</u>	<u>1.19%</u>

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Not expected loss

Not expected loss represents the impact that the capital of the Institution could have derived from unusual losses in the loan portfolio, the level of coverage of this loss for the capital and reserves of an institution is an indicator of solvency adjusted for risk of the same.

Since December 2005, the Institution makes the estimation of the unexpected loss of the credit portfolio operations, using Monte Carlo simulation and analytical methodologies, as of that date the stability of these measures has been observed and its behavior in the face of various changes in the environment, to determine which of them should be used as a measure of the risk of the Institution's loan portfolio.

In November 2007, the IRMC concluded that, of the methodologies proposed for the estimation of the unexpected loss of the loan portfolio, the methodology with an economic approach is the one that best aligns with the basic method based on internal Basel II qualifications, according to:

- The similarity of concepts existing between the proposed economic methodology and the capital requirement for credit risk estimated from the Basel II basic approach. This approach allows institutions to estimate with internal methods the capital requirement necessary to support their risk
- High levels of correlation and similarity in average capital requirement observed during a year of internal implementation of proposals not expected loss of credit portfolio methodologies.

As well, it was considered that the unexpected loss of the loan portfolio should continue to be estimated monthly through the valuation and Monte Carlo methodologies in order to have information regarding future changes in the banking standard in which the valuation is requested. portfolio market. These methodologies are applied in a horizon of one year and with a confidence level of 95%

At the end of December 2017, the estimate of unexpected loss under the economic approach amounts to \$ 17,266 and the credit VaR amounts to \$ 20,125 and represents 8.81% of the portfolio with risk.

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Risk of counterparty and diversification-

In the Institution, an integral control of counterparty risk is exercised, applying the established credit exposure limits. These limits consider the operations throughout the entire balance sheet, that is, both financial markets and the credit portfolio. The methodology used is consistent with the General Rules for the Diversification of Risks in the Realization of Active and Passive Operations Applicable to Credit Institutions. At the end of December 2017, no economic group concentrates credit risk above the maximum financing limits..

As of December 31, 2017, the number of financing exceeding 10% of the basic capital individually is shown below::

Number of financing	Total amount	Capital percentage
28	\$ 207,956	867.3 %

As of December 31, 2017, the amount of financing that is held with the three largest debtors, or, where applicable, groups of people representing common risk, amounts to \$ 53,532.

Operational risk and non-quantifiable

The risks to which a financial institution is exposed are classified into two broad categories; quantifiable and not quantifiable. The quantifiable and non-quantifiable risks, in turn, are divided as shown on the following page.

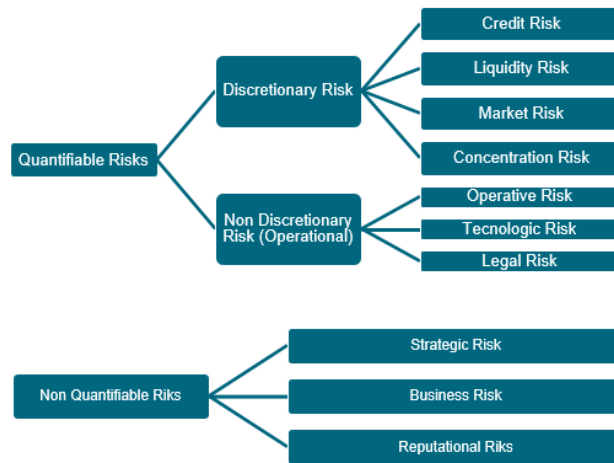
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The non-discretionary risks, that is, the operational risk, are those resulting from the operation of the business, but they are not the result of taking a risk position. These risks are defined below..

- Operational Risk: potential losses derived from failures or deficiencies of internal controls, due to errors in the processing and storage of operations.
- Technological risk: potential losses derived from damages, interruption, alteration or failures derived from the use or dependence on hardware, software, systems, applications, networks and any other channel of information distribution in the provision of banking services with customers of the Institution that derive in errors in the processing and storage of operations or in the transmission of information.
- Legal Risk: potential losses derived from the applicable legal and administrative provisions, the issuance of unfavorable administrative and judicial resolutions and the application of sanctions, in relation to the operations carried out by the institutions.

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Non-quantifiable risks are unforeseen events to which a statistical base cannot be formed to measure potential losses, among which are the following:

- Strategic risk: potential losses by deficiencies in the decision-making process, in the implementation of procedures and actions to carry out the business model and strategies of the institution, as well as lack of knowledge about the risks to This is exposed by the development of their business activity and that affect expected results to achieve the objectives agreed to by the institution in its strategic plan.
- Business risk: potential losses attributable to the inherent characteristics of the business and changes in the economic cycle or environment in which the institution operates.
- Reputation risk: potential losses in the development of the activity of the institution led to the impairment in perception that have the different parties concerned, both internal and external, on its solvency and viability.

The objective of managing operational risk and non-quantifiable risks is to formally establish the rules and policies necessary to systematically and efficiently carry out the identification, measurement, monitoring, limitation, control, information and disclosure of non-discretionary risks and non-quantifiable, to which all areas of the Institution that are involved in activities that imply a non-discretionary or non-quantifiable risk must be attached, as well as the purpose of ensuring the timely identification of the capital requirements and the resources derived from these risks.

The policies for the management of operational risk and non-quantifiable risks are the following:

- It is the responsibility of the Operational Risk Sub-Directorate to define the procedures for the management of inherent and residual operational risks, economic loss events, tolerance levels, risk limits, amounts of probable potential losses derived from judicial resolutions or administrative unfavorable litigation in which the Institution is plaintiff

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- None of the procedures defined for these risks may be modified or altered, only with the authorization of the Integral Risk Management Committee and annually by the Board of Directors.
- The necessary evidence will be available to manage non-discretionary and non-quantifiable risks.
- The tools that have been developed or acquired by the Institution will be used to manage operational risk and non-quantifiable risks.

The strategy for operational risk and non-quantifiable risks is to identify, manage, quantify (if applicable), document the way to mitigate them through risk controls by processes considering the institutional expertise, which could impact or violate the solvency of the Institution above the minimum requirements and with this help in the fulfillment of the institutional goals and objectives. Also to disclose in a timely manner the information of these risks to the Governing Bodies for timely decision-making. Likewise, promote the culture of the administration of these types of risks in the Institution.

The process of operational risks is fundamental and is documented and certified according to the quality management system under the ISO 9001-2015 Standard that contributes to the achievement of the objective of managing the operational risk to which the Institution is exposed.

The Institutional uses the system “Operating risk tool” which captures the information and results from the operational risk monitoring, this system also manages internal and regulatory reports.

The reports related to the operating risk management (including technological and legal) is carried out by the IRMC through “Management report and risk monitoring” on quarterly basis.

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Methodologies, limits and tolerance levels.

Method to determine the capital requirement for operational risk-

The institution uses the basic indicator method to calculate the capital requirement for their exposure to operational risk, following the methodology described in the provisions.

Non-discretionary risks:

Operational risk-

The methodology used for the management of operational risk (quantitative and qualitative analysis) is through an internal institutional model of operational risk, which is based on a scorecard that considers five risk factors. This methodology is applied to the results of the self-evaluations of the processes that describe the Institution's task and allows the comparison of the processes analyzed with two indicators; nature and efficiency, which have defined tolerance levels by risk factor and by indicator.

In addition, the inherent and potential risks of each process are identified, classified and qualified based on the methodology defined by the Banking Commission and the result is sent in an annual report called "Estimation of operational risk levels". The methodology of the Banking Commission provides product catalogs, process, line of business, type of risk and a guide for the calculation of frequency and impact of the inherent risk (without applying controls).

Considering the results obtained, it has been defined that for the inherent inherent risks located in the quadrant nine red zone (high frequency and high impact), together with those responsible for the process to which it belongs, additional actions or controls for its administration will be defined.

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The quantitative analysis is carried out through the events of loss due to operational risk aroused in the institution and whose information is provided by the owners of the processes involved. These events are classified according to the methodology defined by the Commission to carry out the regulatory reports "Events of loss due to operational risk" and "Update of loss events due to operational risk". The methodology of the Banking Commission provides the catalogs of the product, process, line of business and type of risk

For the monitoring of loss events, an operational risk limit was defined considering the positive net income of three years, considering methodologies and comments from the Banking Commission.

Technological risk-

The technological risk methodology to identify, quantify and manage this risk is performed by IT and is based on five indicators which are network security, virus detection and blocking, availability of critical services and non-critical ones. As a control of risk monitoring, IRMC is reported at least quarterly.

Its monitoring is monthly and is carried out by comparing the levels obtained in each indicator that considers the events reported by the areas users against the tolerance levels agreed between the area of computer science and these areas. This risk information is captured by the informatics area directly in operational risk tool.

Legal risk-

There is an internal methodology for estimating the registry of potential losses in terms of legal risk, based on the expectations of specialists to obtain a favorable resolution, classifying them into five bands:

- Without sufficient evidence.
- High.
- Moderate.
- Considerable.
- Low

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The application of the methodology is carried out by the Litigation and Credit Legal Department, the staff identifies, quantifies and manages the legal risk. As a control of risk monitoring, IRMC is reported at least quarterly.

The results of the potential losses are grouped, analyzed and reported, with a periodicity at least quarterly to the IRMC, by type of judgment, which are the following:

- Labour nature
- Contentious portfolio
- Trust
- Commercial
- Treasury and stock trading

Risks on the assets of the institution

They are those derived from casualties or unforeseen external events that cannot be associated with a probability of occurrence and that the economic losses caused can be transferred to external entities that take risks.

<u>Type of risk</u>	<u>Definition</u>	<u>Example</u>
Sinister	Risk of loss due to catastrophic events of nature that can interrupt the operation or affect assets of the institution.	Fire, earthquake, volcanic eruption, hurricane, among others.
External	Risk of loss caused by entities outside the institution.	Vandalism, seedlings, etc.

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For this type of risk, monitoring is carried out considering the following criteria:

Inventory	Control Measures	Economic impact
Institution Assets	Institutional Program for Assurance Assets	Premium payments
Foreclosed Assets	Institutional Program for Assurance Assets	Deductibles in case of materialization.

During the year 2017, were covered, via policy, the damages that occur within the national territory and abroad of tangible and intangible assets (all kinds of software or packages of programs, licenses, permits, technology information and base data) including general damage, civil liability, accidental breakage of glass including neon signs, theft and/or assault with violence or without violence, theft of money and securities, banking, electrical equipment, Electromechanical, electronic, electromagnetic and fixed and mobile telephony, boilers and equipment subject to pressure, breakage of machinery, equipment contractor, goods in transit (transport), works of art, and difficult or impossible to reposition objects, money and values, outfitting and safety equipment, personal accident, infidelity of employees and terrorism; It also has a policy covering the vehicle fleet.

Non-quantifiable risks

The implemented methodologies are in accordance with provisions of the provisions. The next sheet provides a brief description of them.

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- Strategic risk. -The institution has a methodology based on defining, documenting, and follow-up to the Institution's Management strategies, these methodology, each year are defined and approved, as well as presented to the Board of director, at least on a quarterly basis, for the decision making and mitigation of detected risks.
- Business risk. - Four indicators that help to identify the possible materialization of the risks that could affect the Institution derived from movements in the financial medium and the economic cycle were defined as a methodology to manage this risk. These indicators are given monthly monitoring through risk reports
- Reputation risk. - For the administration of this risk, a Communication Plan was defined that applies and monitors the Social Communication Management, said Plan considers the attention of the minimum requirements issued by the Banking Commission in the Provisions regarding the reputation risk. The Social Communication Management monitors the events that affect the negative perception that is held internally or externally of the Institution. As a control of this risk, the IRMC is informed at least quarterly..

Operational risk results:

Results of self-evaluation-

The result of the most relevant processes of the Institution in terms of its nature at the end of December 2017, is as follows:

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<u>Process</u>	<u>Nature Indicator*/</u>	<u>Tolerance Level</u>
Custody and Administration of Securities and Cash	99.83	High risk
Treasury management	98.75	High risk
Cash flow management and control	94.29	High risk
Foreign Exchange market	92.58	High risk
General cashier's office	90.13	High risk
Financial broker Front Office	89.45	High risk
Money market	87.17	High risk
Capital market	85.45	High risk
Recovery of second floor portfolio	81.26	Medium high risk
Credit control desk operation	81.11	Medium high risk
Derivatives market	81.01	Medium high risk
Recovery of first floor portfolios, emerging programs, and ex-employees	80.63	Medium high risk
Financial broker Back Office	69.11	Medium high risk
Securities loan	68.77	Medium high risk
Management of automatic guarantees	68.01	Medium high risk
Management of electronic products	67.89	Medium high risk
Securities safe and central	66.00	Medium high risk
Trustee	61.80	Medium high risk
Provision of contentious legal services and banking formalization	60.23	Medium high risk
Financial Information, Accounting and preparation of Financial Statements	60.20	Medium high risk
Expense operation	55.23	Medium high risk

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The result at the end of December 2017 of the most relevant processes that describe the work of the institution, in term of efficiency is as follows:

<u>Process</u>	<u>Nature Indicator */</u>	<u>Tolerance Level</u>
Financial broker Front Office	43.29	Medium risk
Custody and Administration of Securities and Cash	41.50	Medium risk
Financial broker Back Office	40.86	Medium risk
Foreign Exchange market	40.42	Medium risk
Derivatives market	37.04	Medium risk
Expense operation	36.00	Medium risk
Recovery of second floor portfolio	35.26	Medium risk
Trustee	34.89	Medium risk
Financial Information, Accounting and preparation of Financial Statements	34.80	Medium risk
Treasury management	34.13	Medium risk
Cash flow management and control	34.00	Medium risk
Money market	32.81	Medium risk
Recovery of first floor portfolios, emerging programs, and ex-employees	32.68	Medium risk
Management of electronic products	32.61	Medium risk
Capital markets	31.16	Medium risk
Management of automatic guarantees	28.46	Medium risk
Credit control desk operation	27.74	Medium risk
General cashier's office	26.19	Medium risk
Securities safe and central file	24.67	Medium risk
Provision of contentious legal services and banking formalization	24.26	Medium risk
Securities loan	20.91	Low risk

*/ The higher score, the more critical in terms of efficiency of the process

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During 2017, no inherent potential operational risk was identified in the red zone, ie zone nine (high frequency and high impact), so the established risk limit was met.

Results of the events of economic losses.

During the year 2017, forty-five loss events were accounted for by operational risk with a likely impact of \$12.23. The monthly average was four events with an amount of \$1.01.

<u>Quarter</u>	<u>Number of events</u>	<u>Likely economic impact</u>	<u>% of LEI (IEP) each quarter</u>	<u>Average amount per month event</u>
First	12	0.35	2.86%	0.12
Second	5	0.24	1.94%	0.08
Third	16	11.46	93.73%	3.82
Fourth	12	0.18	1.47%	0.06
Total	45	12.23	100%	

The consumption of the limit of the events of economic loss at the end of each month of year 2017 was within the established parameters, with the exception of September, where it held an exhibition of \$10.99.

Result of technological risk indicators

During the twelve months of 2017, the indicator level of security to the network had zero intrusions, the indicator of recovery of critical services under disaster drills had 100% of behavior, likewise, the indicator detection and blocking of virus to the network had zero impacts. The quarterly and monthly average of these three risk indicators were located in the defined goal

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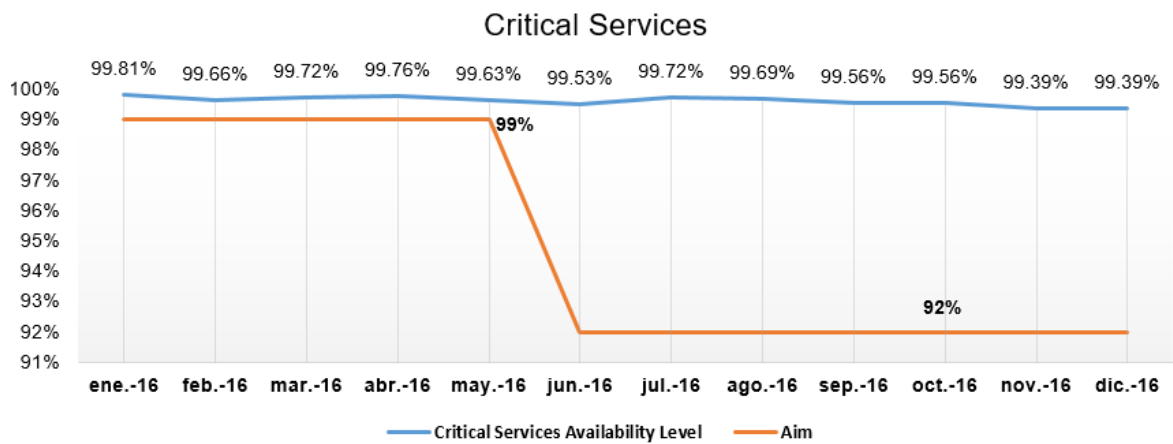
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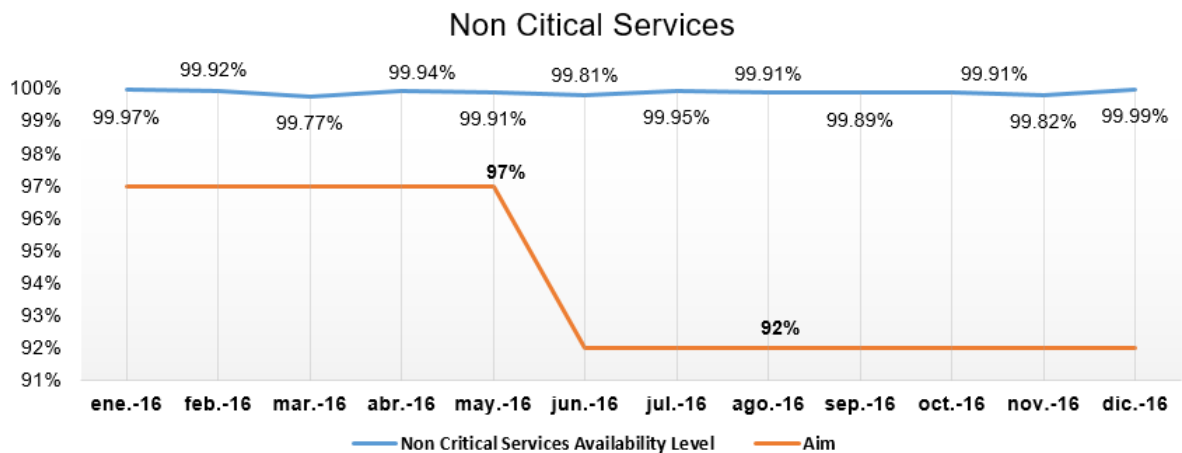
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The behavior of the indicator of availability of critical services in the twelve months of year 2017 is as follows:



The behavior of the availability of non-critical services indicator in the twelve months of the year 2017, is as follows:



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The five technological risk indicators were found within the goals established for the management of this risk.

During the year 2017, annual average and quarterly average behavior of the indicators; Availability of critical services and the availability of non-critical services were as follows:

T.R. indicator <u>Description</u>	1st Quarter <u>2017</u>	2nd Quarter <u>2017</u>	3rd Quarter <u>2017</u>	4th Quarter <u>2017</u>	2017 <u>Average</u>
Availability level of critical services	99.73%	99.64%	99.66%	99.44%	99.62%
Availability level of non-critical services	99.89%	99.89%	99.92%	99.91%	99.90%

The quarterly and monthly average of the availability level of critical and non-critical services were within the established goals.

Result of the legal risk-

At the end of December 2017, the state that keeps the record of potential losses in terms of legal risk is the following:

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<u>Type of lawsuit</u>	<u>Contingency</u>	<u>Provision</u>	<u>Provision/ Contingency</u>	<u>Income Loss</u>	<u>Income or loss Provision</u>
Total (1+2+3+4)	\$ 131.71	47.11	35.75%	\$14.50	30.79%
1) Labor nature	32.81	17.33	52.82%	9.67	55.81%
2) Litigation portfolio	12.55	11.30	90.04%	4.67	41.31%
3) Trusts	86.35	18.48	21.40%	0.16	0.87%
4) Treasury and securities trading	0.00	0.00	0.00%	0	0.00%

Non-quantifiable risks

Results in the affectations to the patrimonial assets of the Institution: During the year 2017, five claims were reported that affected the patrimonial assets of the Institution in the branch related to electronic and diverse equipment, with an estimated amount of \$ 0.04..

Strategic risk: During the year of 2017, at least quarterly monitoring of the compliance behavior of senior management goals has been carried out to identify, in an expert manner, the main risks in order to mitigate them and make decisions that do not cause failure to comply with the Institution's goals.

Business risk: During the year 2017, the indicators defined for the administration of this risk were monitored, through market risk, concentration, liquidity, guarantees and credit reports.

Reputation risk: During year 2017, the Social Communication Management met the minimum requirements in terms of reputation risk issued by the Banking Commission in the Provisions, additionally monitored events that affect the negative perception that is held both internally and externally on a monthly basis, analyzing the positive and negative notes via printed, electronic communication channels, internet portals and state information

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Leverage ratio

The information related to leverage is disclosed with figures as of December 2017, in compliance with the Resolution that modifies the general provisions applicable to credit institutions, published by *Diario Oficial de la Federación* (Official Gazette) on June 22, 2016, article 2 Bis 120, articles 180, 181 and annex 1 - O Bis:

**TABLE I.1
STANDARDIZED DISCLOSURE FORMAT FOR THE LEVERAGE RATIO**

REFERENCE	CATEGORY	AMOUNT
Exhibitions in the balance		
1	Items on the balance sheet (excluding derivative financial instruments and repurchase and securities lending operations -SFT by its acronym in English- but including the collateral received as guarantee and recorded in the balance sheet	496,505
2	(Amounts of assets deducted to determine the level 1 of Basel III capital)	-
3	Exhibitions within the balance sheet (net) (excluded derivative financial instruments and SFT, sum of lines 1 and 2)	496,505
Exposure to derivative financial instruments		
4	Current replacement cost associated with all operations with derivative financial instruments (net of the margin of variation in admissible cash)	-
5	Amounts of additional factors due to future potential exposure, associated with all operations with derivative financial instruments	2,809
6	Increase in collateral contributed in operations with derivative financial instruments when said collaterals are derecognized from the balance sheet in accordance with the operating accounting framework	N.A.
7	(Deductions to accounts receivable for variation margin in cash contributed in operations with derivative financial instruments)	-
8	(Exposure due to transactions in derivative financial instruments on behalf of clients, in which the settlement partner does not grant its guarantee in case of breach of the obligations of the Central Counterparty)	N.A.
9	Adjusted notional cash amount of the credit derivative financial instruments subscribed	N.A.
10	(Compensations made to the adjusted notional cash of the credit derivative financial instruments subscribed and deductions of the additional factors by the credit derivative financial instruments subscribed)	N.A.

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11	Total exposure to derivative financial instruments (sum of lines 4 and 10)	2,809
Exhibitions for financing transactions with securities		
12	Gross SFT assets (without recognition of compensation), after adjustments for accounting transactions for sales	15,406
13	(Accounts payable and receivable from SFT compensated)	-12,688
14	Counterparty Risk Exposure by SFT	317
15	Exhibitions by SFT acting on behalf of third parties	-
16	Total exhibitions by financing values (sum of lines 12 to 15)	3,035
Other off-balance sheet exposures		
17	Exhibition out of balance (gross notional amount)	135,190
18	(Adjustments for conversion to credit equivalents)	-121,671
19	Items out of balance (sum of lines 17 and 18)	13,519
Capital and total exposures		
20	Tier 1 capital	26,786
21	Total exhibitions (sum of lines 3, 11, 16 and 19)	515,868
Leverage ratio		
22	Basel III leverage ratio	5.2%

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**TABLE II.1
ADJUSTED ASSETS AND TOTAL ASSETS COMPARATIVE**

REFERENCE	DESCRIPTION	AMOUNT
1	Total assets	529,092
2	Adjustment for investments in the capital of banking, financial, insurance or commercial entities that are consolidated for accounting purposes, but are outside the scope of regulatory consolidation	-
3	Adjustment related to trustee assets recognized in the balance sheet in accordance with the accounting framework, but excluded from the exposure measure of the leverage ratio	N.A.
4	Adjustment for derivative financial instruments	-14,371
5	Adjustment operations of repurchase/resell agreements and securities lending	-12,372
6	Adjustment for items recognized in balance sheet	13,519
7	Other adjustments	-
8	Exhibition of the leverage ratio	515,868

**TABLE III.1
RECONCILIATION OF TOTAL ASSETS AND EXPOSURE WITHIN THE BALANCE**

REFERENCE	CONCEPT	AMOUNT
1	Total assets	529,092
2	Transactions in derivative financial instruments	-17,180
3	Operations in repurchase/resell and loan securities	-15,406
4	Trustee assets recognized in the balance sheet in accordance with the accounting framework, but excluded from the exposure measure of the leverage ratio	N.A.
5	Exhibitions in the Balance	496,505

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TABLE IV.1

MAIN CAUSES OF THE MAJOR VARIATIONS OF THE ELEMENTS

(NUMERATOR AND DENOMINATOR) OF LEVERAGE RATIO

CONCEPT/QUARTER	Nov 17	Dec 17	VARIATION (%)
Basic capital	24,355	26,786	10.0%
Adjusted assets	525,671	515,868	-1.9%
Leverage ratio	4.6%	5.2%	12.1%

(27) Recently issued financial reporting standards

Changes in the provisions of the Banking Commission

On December 27, 2017, the Banking Commission published in the Official Gazette various modifications to the Accounting Criteria. These changes will be effective on January 1, 2019, Management is in the process of evaluating the effects that these modifications will have on the financial information. Most relevant changes are shown below:

Criterion A-2 “Application of particular rules

Certain MFRS issued by the CINIF are incorporated, with the purpose of being applicable to the credit institutions, so as the term for its application, in order for credit institutions to comply with them. Mentioned MFRS are the following: B-17 “Fair value determination”, C-16 “Impairment of financial instruments receivable”, C-19 “Financial instruments payable”, C-20 “SPPI Financial instruments”, D-1 “Revenue from contracts with customers” and D-2 “Costs from contracts with customers”.

Criterion B-6 “Loan portfolio” and D-2 “Income statement”

Accounting Criteria for credit institutions are adjusted so these institutions be able to cancel, in the period of occurrence, excess of allowance for loan losses, as well as to recognize recovery of loans previously impaired in the “allowance for loan losses” caption in the consolidated income statement

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Derived from the modification mentioned in the previous paragraph, and in compliance with the resolution established, the Bank has chosen to early adopt the Criterion, affecting its financial statements at January 31, 2018, prospectively...

Standards recently issued by the CINIF

The CINIF has issued the MFRS and improvements listed below:

MFRS B-17 “*Determination of fair value*”- effective for years beginning on or after January 1, 2018 (January 1, 2019 for credit institutions). Changes in valuation or disclosure have to be recognized prospectively. It establishes the valuation and disclosure standards in the determination of fair value, in initial and subsequent recognition, if the fair value is required or allowed by other specific MFRS

MFRS C-16 “*Impairment of financial instruments receivable*”- effective for years beginning on January 1, 2018 (January 1, 2019 for credit institutions) with retrospective effects. It establishes standards for the accounting recognition of impairment losses of all financial instruments receivable; it indicates when and how an expected impairment loss should be recognized and establishes the methodology for determination.

The primary changes arising from this MFRS consist of determining when and how expected impairment losses on financial instruments receivable should be recognized, including:

- It establishes that impairment losses on financial instruments receivable should be recognized if the credit risk increases and thus it is concluded that a portion of future cash flows of the financial instruments receivable will not be recovered.
- It proposes recognizing the expected loss based on the entity's historical experience of credit losses, current conditions and reasonable and supportable forecasts of the various quantifiable future events that could affect the amount of future cash flows of the financial instruments receivable.
- With regard to interest-bearing financial instruments receivable, it establishes estimating how much of the financial instruments receivable amount is deemed recoverable and when, since the recoverable amount must be recorded at present value.

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MFRS C-19 “Financial instruments payable” - effective for years beginning on or after January 1, 2018 (January 1, 2019 for credit institutions) with retrospective effects. Some of the main points covered by this MFRS include the following

- It provides for the possibility of measuring, subsequent to their initial recognition, certain financial liabilities at fair value when certain conditions are fulfilled.
- Long-term liabilities are initially recognized at present value.
- In restructuring a liability, without the future cash flows for its settlement being substantially modified, the costs and commissions expensed in this process shall affect the amount of the liability and be amortized on a modified effective interest rate basis instead of directly affecting net income or loss.
- It includes the provisions of IFRIC 19 “Extinguishing Financial Liabilities with Equity Instruments”, which was not provided for by the existing standard.
- The effect of extinguishing a financial liability should be presented as financial income (loss) in the comprehensive statement of income.
- It introduces the concepts of amortized cost in valuing financial liabilities and of the effective interest method based on the effective interest rate.

MFRS C-20 “SPPI Financing instruments receivable” - effective for years beginning January 1, 2018 (January 1, 2019 for credit institutions), and is applicable retrospectively. Some of the main aspects resulting from the adoption of this MFRS are as follows:

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- Classification of financial instruments within assets. To determine such classification, the concept of intention to acquire and hold financial instruments has been removed. Instead, the concept of business management model is adopted, either for obtaining a contractual yield, generating a contractual yield and selling in order to achieve certain strategic objectives, or generating earnings from the purchase and sale thereof, in order to classify them in accordance with the respective model.
- The valuation effect of investments in financial instruments is also focused on the business model.
- The reclassification of financial instruments is not permitted among receivables, strategic investments, and negotiable instruments, unless the entity changes its business model.
- An embedded derivative that modifies the cash flows of principal and interest is not separated from its host receivable financial instrument. The entire receivable financial instrument shall be measured at fair value, as if it were a negotiable financial instrument.

MFRS D-1 “Revenue from contracts with customers”- establishes standards for the accounting recognition of revenues arising from contracts with customers and is effective for periods beginning on or after January 1, 2018 (January 1, 2019 for credit institutions), and is applicable retrospectively. It eliminates the supplementary application of International Accounting Standard (IAS) 18 “Revenues”, SIC 31 “Revenues – Barter transactions of advertising services”, IFRIC 13 “Customer Loyalty Programs”, and IFRIC 18 “Transfers of assets from customers”. Additionally, this MFRS, along with MFRS D-2, repeals Bulletin D-7 “Construction and manufacturing contracts of certain capital goods” and IFRS 14 “Construction, sales and service contracts related to real estate”. Some of the primary changes are the following:

- The transfer of control as basis for the opportunity of revenue recognition is established.
- The identification of the obligations to be fulfilled in a contract is required.

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- It indicates that the transaction amount between obligations to fulfill must be assigned based on independent sales prices.
- The concept “conditional account receivable” is introduced.
- The recognition of collection rights is required.
- Requirements and guidance on how to value the variable consideration and other aspects, upon valuing the income are established.

MFRS D-2 “Costs from contracts with customers”- establishes rules for the accounting recognition of costs of sales of goods or provision of services. This is effective for periods starting on or after January 1, 2018 (January 1, 2019 for credit institutions), and is applicable retrospectively. Along with MFRS D-1 “*Revenues from contracts with customers*”, it repeals Bulletin D -7 “*Construction and manufacturing contracts of certain capital goods*” and IFRS 14 “*Construction, sales and service contracts related to real estate*”, except regarding the recognition of assets and liabilities in this type of contracts within the scope of other MFRS.

The primary change is the separation of the standard related to the recognition of revenues from contracts with customers, from the standard corresponding to the recognition of costs for contracts with customers. Additionally, it extends the scope of Bulletin D-7, referring exclusively to costs related to construction and manufacturing contracts for certain capital goods, to include costs related to all types of contracts with customers.

As explained before, the Banking Commission established January 1, 2019 as the effective date of application of the mentioned MFRS, Management is in the process of evaluating their impacts.

MFRS C-3 “Accounts receivable”- effective for years beginning on or after January 1, 2018, with retrospective effects, except for the valuation effects that may be prospectively recognized, if it is impractical to determine the effect on each one of the prior periods presented. Some of the primary changes presented are the following:

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- It provides that accounts receivable based on a contract are deemed financial instruments, while some other accounts receivable, resulting of legal or tax provisions, may have certain characteristics of a financial instrument, such as bearing interest, but are not in themselves financial instruments.
- It provides that the allowance for doubtful trade receivables shall be recognized as revenue is earned, based on the expected credit losses, and the allowance shall be recorded as an expense, separately when significant, in the statement of comprehensive income.
- It provides that, upon initial recognition, the time value of money shall be considered. Therefore, should the effect of the present value of the account receivable be significant in light of the term, an adjustment must be made taking into consideration such present value.
- It requires a reconciliation between the beginning and ending balances of the allowance for doubtful accounts for each period presented.

Management estimates that the adoption of this new MFRS will not generate important effects, since there are specific Criteria (B-6 “Loan portfolio” and A-2 “Application of particular rules”) established by the Banking Commission

MFRS C-9 “Provisions, Contingencies and Commitments”- effective for years beginning on or after January 1, 2018. It supersedes Bulletin C-9 “Liabilities, Provisions, Contingent Assets and Liabilities and Commitments”. The first-time adoption of this MFRS does not result in accounting changes in the financial statements. Some of the primary aspects covered by this MFRS include the following:

- The scope is narrowed by relocating the topic concerning accounting for financial liabilities to MFRS C-19 “Financial instruments payable”.
- The definition of “liability” is modified by eliminating the qualifier “virtually unavoidable” and including the term “probable”.

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- The terminology used throughout the standard is updated to standardize the presentation with the rest of the MFRS.

2018 MFRS Revisions

In December 2017, the CINIF issued a document called “2018 MFRS Revisions” containing precise modifications to some of the existing MFRS. The main revisions that bring about accounting changes are mentioned in the next page.

MFRS B-10 “Effects of inflation”- Requires disclosing the percentage of accumulated inflation for the three previous fiscal years that served as the basis to describe the economic environment in which the entity operated in the current year as inflationary or non-inflationary, and the cumulative inflation percentage of three years, including the two previous years and that of the period itself, which will serve as a basis for rating the economic environment in which the entity will operate in the following year. This revision will be effective for periods starting on or after January 1, 2018, allowing early adoption. The resulting accounting changes should be recognized retrospectively.

MFRS C-6 “Property, plant and equipment” and FRS C-8 “Intangible assets”- Establishes that a method of depreciation and amortization of an asset based on the generation of economic benefits associated with its use is not appropriate, given that said amount may be affected by factors other than the pattern of consumption of economic benefits of the asset. Clarifies the meaning of the concept of consumption of future economic benefits of an asset. This revision will be effective for periods starting on or after January 1, 2018, allowing early adoption. The resulting accounting changes should be recognized prospectively

MFRS C-14 “Transfer and recognition of financial assets”- Eliminates the requirement to recognize in earnings the effects of the subsequent recognition at fair value of a transferred asset and of the associated liability since it represented a contradiction with the requirement in the same standard that said recognition be made based on the relative rules, depending on the type of asset in question. This revision will be effective for periods starting on or after January 1, 2018, allowing early adoption. The resulting accounting changes should be recognized retrospectively.

Management estimates that the adoption of MFRS revisions will not generate important effects.

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(28) Approval of the financial statements-

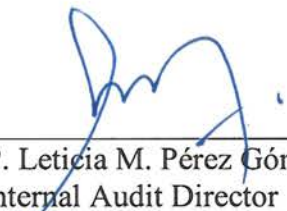
On February 16, 2018, the officers who signed the consolidated financial statements, authorized the issuance of the accompanying consolidated financial statements and related notes. These accompanying notes are part of the consolidated financial statements at December 31, 2017 and 2016.



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Deputy General Director of
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EXHIBIT C

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The information in this report was compiled by the Financial Planning and Programing Department.

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