INTER-AMERICAN DEVELOPMENT BANK

ANNUAL REPORT 2006

FINANCIAL SUMMARY 2002–2006

ORDINARY CAPITAL

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

	2006	2005	2004	2003	2002
Operational Highlights					
Loans and Guarantees Approved	$ 5,774	$ 6,738	$ 5,468	$ 6,232	$ 4,143
Loan Disbursements	6,088	4,899	3,768	8,416	5,522
Loan Repayments	8,615	5,224	5,199	7,279	4,106
Balance Sheet Data					
Cash and Investments–Net, After Swaps	$ 16,051	$ 13,717	$ 13,046	$ 14,855	$ 14,780
Loans Outstanding	45,932	48,135	49,842	50,655	47,958
Undisbursed Portion of Approved Loans	16,080	17,000	16,093	15,619	18,570
Total Assets	66,475	65,382	67,346	69,669	65,031
Borrowings Outstanding, After Swaps	43,550	43,988	45,144	49,275	48,179
Equity	19,808	18,727	18,511	17,112	14,269
Income Statement Data					
Loan Income	$ 2,466	$ 2,413	$ 2,498	$ 2,711	$ 2,639
Investment Income	619	403	288	298	319
Borrowing Expenses, After Swaps	2,070	1,733	1,572	1,636	1,842
Operating Income	627	712	862	2,434	727
Ratio					
Total Equity to Loans Ratio (TELR)	40.8%	37.3%	36.1%	33.0%	30.9%

FUND FOR SPECIAL OPERATIONS

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

	2006	2005	2004	2003	2002
Operational Highlights					
Loans and Guarantees Approved	$ 605	$ 410	$ 552	$ 578	$ 406
Loan Disbursements	398	424	463	486	313
Loan Repayments	290	301	294	296	256
Balance Sheet Data					
Cash and Investments, Net	$ 1,592	$ 1,564	$ 1,559	$ 1,591	$ 1,616
Loans Outstanding	7,115	6,873	7,041	7,216	6,763
Undisbursed Portion of Approved Loans	2,229	2,051	2,083	2,000	1,920
Total Assets	9,530	9,386	9,662	10,044	9,845
Fund Balance	9,140	9,041	9,194	9,622	9,520
Income Statement Data					
Loan Income	$ 152	$ 149	$ 145	$ 153	$ 115
Technical Cooperation Expense	19	28	31	23	31
HIPC Debt Relief	(5)	76	486	37	38
Excess of Income Over Expenses (Expenses Over Income)	105	(3)	(413)	53	12

LETTER OF TRANSMITTAL

As required under the By-laws of the Inter-American Development Bank, the Board of Executive Directors hereby submits to the Board of Governors the Annual Report of the Bank for 2006. The Report contains a brief summary of the economic situation of Latin America and the Caribbean and a review of the Bank's operations in 2006.

In addition, the Report contains a description of the Bank's operations—loans, guarantees and grants—; Management's Discussion and Analysis: Ordinary Capital; the financial statements of the Bank; and its general appendices.

January 26, 2007

Annual Report 2006

INTER-AMERICAN DEVELOPMENT BANK

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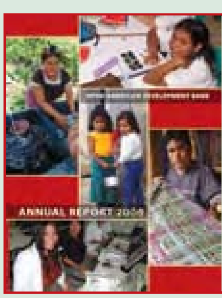
NOTE: The complete Annual Report, including Management's Discussion and Analysis and the audited Financial Statements, is published in the CD-ROM attached to the inside back cover of this report. The Annual Report is also available on the Bank's website at **www.iadb.org**.



COVER PHOTOS • (clockwise from upper left): GUATEMALA • Clean water in Huehuetenango reduces the risk of waterborne disease; at-risk youth in Guatemala City receive job training linked to labor market demand; a microentrepreneur in San Antonio Ilotenango produces textiles thanks to a microloan; girls in Guatemala City learn computer skills that will help them enter the labor market. Center: children in Huehuetenango.

ABOVE • GUATEMALA • Weaver in Chimaltenango who benefited from business services supplied by a private foundation that supports rural women.

ADDITIONAL MATERIAL IN CD-ROM

Financial Statements

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MESSAGE FROM THE PRESIDENT

LUIS ALBERTO MORENO
IDB PRESIDENT

Two thousand six was a year of progress and change for Latin America and the Caribbean, and also for the Inter-American Development Bank Group.

The economic growth rate for Latin America and the Caribbean continued upward in 2006, with regional GDP increasing by an estimated 5.3 percent, based on both a favorable external environment and the consolidation of macroeconomic reform and stabilization. The overall economic news was good, with positive trends in unemployment, inflation, domestic investment and the generation of larger surpluses by central governments. One particularly encouraging sign was the decline in poverty rates: overall, the percentage of the region's population living in poverty fell below 40 percent for the first time since 1980, more than a generation, and the share of those living in extreme poverty, on less than $2 per day, fell to 15 percent. On a less positive note, the region as a whole continued to lag behind other parts of the world, notably Asia, in competitiveness.

The Bank delivered a solid and innovative lending program. Approvals of loans and guarantees—127 projects for nearly $6.4 billion—were up in terms of the number of operations but slightly lower in volume compared with 2005. Disbursements at the Bank in 2006 totaled nearly $6.5 billion, a 22 percent increase over the previous year. The Inter-American Investment Corporation enjoyed the best year in its 17-year history, achieving record loan approvals of $338 million, while keeping administrative costs virtually unchanged. At the Multilateral Investment Fund, following the IDB Board of Governors' approval of a capital replenishment in 2005, project approvals were $125 million, primarily in grants, an 11 percent increase relative to the previous year.

At the Inter-American Development Bank Group, the year was also marked by significant change and innovation. The Bank launched a number of major new programs during the year, chief among them the Opportunities for the Majority initiative, which reflects a shift in emphasis from the macroeconomic to the microeconomic. Opportunities for the Majority is predicated on the need to create strategic partnerships among a number of key actors in development, aligning the interests of the private sector, civil society and communities and acknowledging that past approaches to financing development projects may have proven too monolithic to achieve measurable, sustainable impacts for the estimated 360 million people in our region with incomes of less than $280 per month.

A second major innovation consisted of the Board of Governors' approval of guidelines to implement an expansion in the lending program to subnational entities without a sovereign guarantee, whether private, state-owned or of mixed-capital ownership. The opening of this line, with such vast potential, reflects the Bank's desire to demonstrate an agility and responsiveness to markets and possibilities that it has not heretofore been able to offer.

Two other initiatives fundamental to the Bank's aim of improving economic and social conditions for the region were the creation of the $20 million InfraFund to identify and develop major infrastructure projects and the $10 million Disaster Prevention Fund to assist countries in identifying the risks associated with natural disasters, which directly affect some four million people in the region each year.

A Sustainable Energy Initiative will help the region to lessen its dependence on hydrocarbons. Among the program's ambitious goals will be the introduction of new financing tools for investment in renewable sources of energy and improving access to the carbon finance markets for the IDB's 26 borrowing member countries.

At the end of the year, the Board of Executive Directors approved a resolution to realign the organizational structure of the Bank to enable it to meet strategic challenges. The realignment of the Bank establishes four vice presidencies, for Countries, Knowledge and Sectors, Private Sector and Nonsovereign Guaranteed Operations, and Finance and Administration. We will move forward aggressively to ensure that the changes achieve our objectives—to improve our relevance amid changing economic realities in the region and to make us more results-focused.

A year ago, I reflected on the extraordinary circumstance of 12 countries in Latin America and the Caribbean holding presidential elections in 2006. The voters of these countries did indeed speak. While in a number of cases they ratified the success of a course of policy choices already underway—endorsing fiscal restraint and efforts to keep inflation in check—in others they also gave voice to the poor and the excluded, to bring the majority into the economic and social mainstream. It is the job of the IDB Group, in partnership with our member countries, to seek to help accomplish this same thing, in a way that is not only just, but lasting. I believe that we have laid a good foundation and made a good beginning. The challenge now is to convert plans into actions and to deliver the benefits we are all so understandably eager and impatient to provide.

Luis Alberto Moreno
President
Inter-American Development Bank

BOARD OF EXECUTIVE DIRECTORS

Board members: [from left, front row] Luis Linde, Adina Bastidas, Jaime Quijandría, Eugenio Díaz-Bonilla, Agustín García-López, Tsuyoshi Takahashi, Héctor E. Morales and Hugo Cáceres
[Middle row] Giorgio Leccesi, Fernando Eleta, Ina-Marlene Ruthenberg, Winston A. Cox, Jill Johnson, Martín Bès, Juan E. Notaro Fraga, Jan E. Boyer, Nelly Lacayo-Anderson and Charles Bassett
[Back row] Olivier Myard, Luis Guillermo Echeverri, Alejandro Foxley, Rogério Studart, Hugo Noé Pino, Stewart Mills, Jerry Christopher Butler, Roberto B. Saladín and Arlindo Villaschi
Not pictured: Gustavo Palacio

The IDB shareholders—its 47 member countries—are represented by the Board of Governors, the highest decision-making authority of the Bank. The Governors delegate many of their powers to the Board of Executive Directors, whose 14 members they elect or appoint for three-year terms. The Executive Directors for the United States and Canada represent their own countries; all others represent groups of countries. The Board of Executive Directors also includes 14 Alternates, who have full power to act when their principals are absent. The Board has six committees to review proposals, reports and other documents.

The Board of Executive Directors is responsible for day-to-day oversight of the Bank's operations. It establishes the institution's policies, approves projects, sets interest rates for Bank loans, authorizes borrowings in the capital markets and approves the institution's administrative budget. The work of the Board of Executive Directors is guided by the Regulations of the Board of Executive Directors and the Code of Ethics for Executive Directors.

The agendas and minutes of the Board of Executive Directors' meetings are public documents, as is the Board's annual work program with its quarterly updates.

THE ANNUAL REPORT IS PRODUCED BY THE PUBLIC INFORMATION AND PUBLISHING SECTION OF THE IDB OFFICE OF EXTERNAL RELATIONS.

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This Report can be accessed online at **www.iadb.org**.

The IDB welcomes feedback on the Annual Report. Please send your comments to **alexandrarb@iadb.org**.

Printed on recycled paper

Latin America and the Caribbean in 2006

GUATEMALA • Gourmet variety coffee berries grown in southwestern Guatemala will boost income for small farmers.

ARGENTINA • **Concrete breakwaters are lowered into the harbor at Concepción del Uruguay as part of a port improvement project to increase trade.**

LATIN AMERICA AND THE CARIBBEAN IN 2006

In a favorable international environment, Latin America and the Caribbean had its fourth consecutive year of rising per capita output, low inflation and fiscal and macroeconomic stability in nearly all countries. While commodity prices and international lending terms were unusually favorable, some of the credit goes to domestic policies that successfully maintained macroeconomic discipline during closely contested elections in many countries.

Nevertheless, several of the countries in the region have declined in world competitiveness rankings in recent years, and, while poverty has retreated, unemployment and job quality have not improved substantially. Serious challenges therefore remain, beyond shoring up macroeconomic gains, in strengthening the investment climate, mainstreaming the poor into high-productivity sectors and making social policies more efficient.

INTERNATIONAL ENVIRONMENT

For the third consecutive year, the world economy grew nearly 5 percent in 2006 as a result of strong performance in all major regions. In the United States, growth of 3.3 percent has begun to show signs of flagging economic activity, while the pace of growth in the euro zone quickened to 2.5 percent. China and India maintained very high growth rates (see Figure 1). World trade continued to flourish in such an environment, as it has in recent years, growing by 15 percent.

Primary commodity prices rose sharply in the first half of 2006, but in the second half of the year the price of oil declined to its previous year's level (see Figure 2). Copper prices tapered off as well, but still held well above previous years. Industrial metals continued to see rising prices, while farm produce showed no marked trend.

MEXICO • New facilities in Ixtapa attract tourists and increase foreign exchange earnings.

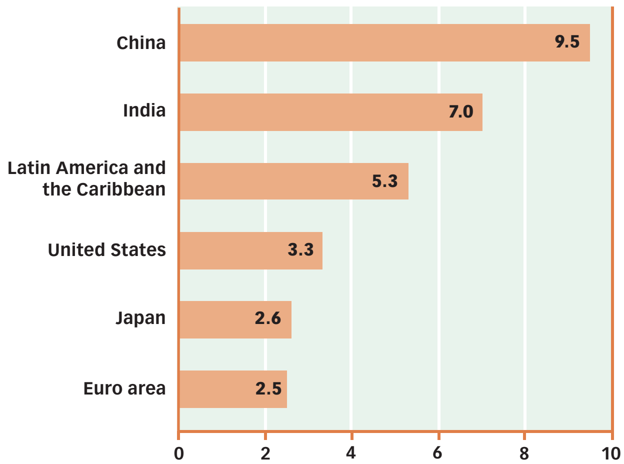
International financial market conditions were very favorable for borrowing countries in 2006, although signs of volatility had been apparent since midyear. Spreads above the U.S. Treasury rate for sovereign bonds issued by emerging economies continued the downward trend of previous years to an all-time low of 205 basis points in April. Thereafter they fluctuated within a 60-basis-point band with no clear tendency. At the same time, however, the rate on 10-year U.S. Treasury notes dropped by some 60 basis points after peaking at 5.2 percent in July.

Although Latin American bond spreads reflected these trends, the gaps between countries narrowed. On the last trading day of 2006 (December 29), the sovereign bond margins over U.S. Treasuries were 84 basis points for Chile, 100 for Mexico, 118 for Peru, 161 for Colombia, 192 for Brazil, 182 for Venezuela and 216 for Argentina (see Figure 3). While the instability observed at times in 2006 may have been associated with domestic political events, it does point to heightened sensitivity in world financial markets.

MAIN MACROECONOMIC OUTCOMES

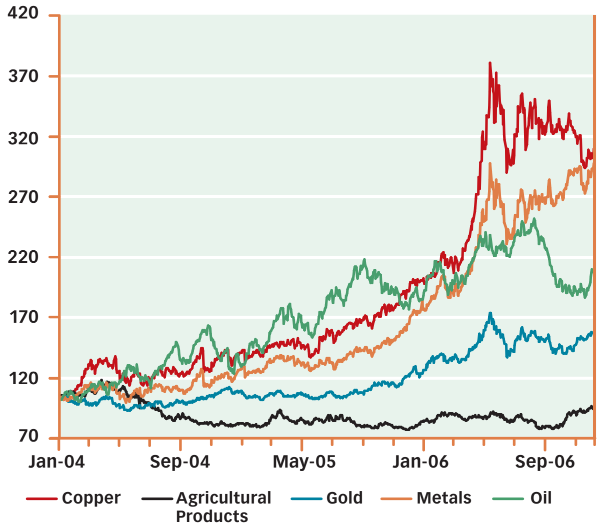
Latin America and the Caribbean posted growth of 5.3 percent in 2006, up slightly from the previous year, leading to a 3.8 percent increase in per capita output in 2006 and a 12 percent increase since 2002 (see Table I). Growth rates were largely homogenous across countries, although

FIGURE 1. GROSS DOMESTIC PRODUCT GROWTH, 2006
(Percentage variation)



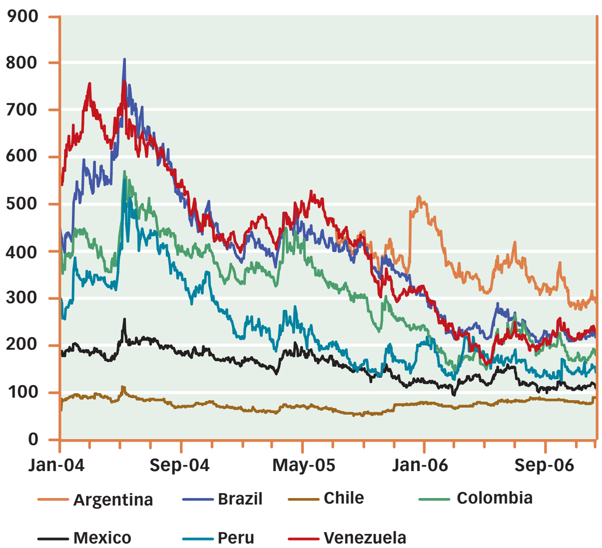
Sources: ECLAC, *Preliminary Overview of the Economies of Latin America and the Caribbean*, 2006, and LatinFocus, January 2007.
Note: All calculations are based on the most recent projections available, since the official figures have not yet been processed.

FIGURE 2. COMMODITY PRICES, 2004–2006
(January 2004 = 100)



Source: Bloomberg.

FIGURE 3. FINANCIAL CONDITIONS, 2004–2006
(Spreads compared with U.S. Treasury Bonds)



Source: Bloomberg.

those in Argentina, the Dominican Republic, Panama, Peru, Trinidad and Tobago, Uruguay, and Venezuela exceeded 7 percent.

The international environment has certainly been a decisive factor in the region's economic growth. But credit is also due to the policies adopted by governments to maintain macroeconomic stability and enhance the business climate. However, only a few of the region's countries have seen their global competitiveness rankings improve in the last two years, as described in the section of this report on competitiveness. A major effort is still needed in most countries to create conditions more conducive to private investment.

Estimated average inflation in the region was 4.8 percent in 2006, continuing the downward trend initiated in 2003. Although Argentina, Haiti, Trinidad and Tobago, and Venezuela saw prices rise 10 percent or more, inflationary pressures receded in almost every other country (see Table I).

In a context of high economic growth, low government bond rates and high export prices, it is not surprising that a majority of the region's countries maintained a strong fiscal position. The estimated average central government deficit was just 0.3 percent of GDP, almost 1 percent of GDP lower than the previous year and 3 percent of GDP below the figure for 2001. This performance is noteworthy because it comes at a time of intense election activity under circumstances that in the past have often led to unsustainable public spending.

There are several indications that fiscal policies have advanced in the region. The fiscal responsibility mechanisms introduced between 1999 and 2004 by Argentina, Brazil, Chile, Colombia, Ecuador, Panama, Peru and Venezuela, which have achieved varying degrees of success, and a firmer political commitment to fiscal soundness deserve credit for this result. Total debt ratios are falling throughout the region (see Table I), and the debt mix is shifting toward domestic debt denominated in local currencies. But dollar-denominated debt is still high in the region, and indebtedness in some countries is still so heavy as to potentially jeopardize fiscal and macroeconomic stability.

The region ended 2006 with a current account surplus equivalent to 1.8 percent of GDP, slightly higher than last year. The majority of countries maintained manageable external positions, running at most a slight deficit. However, current account deficits of 4 percent of GDP or higher are still present throughout Central America, with the exception of Honduras. Strong export performance has been a decisive factor in the favorable external results, and the key driver of economic growth for a number of countries. Latin American exports grew 21.4 percent in 2006, the fourth consecutive year of similar growth. Intraregional exports rose by 24.5 percent and extraregional exports by 20.8 percent. Apart from favorable external conditions, exports were buoyed by the many intraregional and extraregional trade agreements that have entered into effect in recent years.

This year Peru and Colombia concluded negotiation of free trade agreements with the United States. Substantial progress was made on trade negotiations between several Latin American and Caribbean countries and several Asian countries and between subregional trade groups in the region and the European Union. Noteworthy within the region itself was Venezuela's decision to withdraw from the Andean Community of Nations and join MERCOSUR.

LABOR AND SOCIAL OUTCOMES

Average unemployment rates for the region changed very little in 2006. Apart from Venezuela, where unemployment declined more than two percentage points, improvements in other countries were small, and Brazil saw a slight

TABLE I • LATIN AMERICA AND THE CARIBBEAN: MAIN MACROECONOMIC RESULTS, 2006

	GDP Growth (%)	Inflation (%)	Current Account (% GDP)	Public Debt (% GDP)*
Argentina	8.5	10.0	4.0	78.2
Bahamas	4.0	2.5	n.a.	37.0
Barbados	3.8	7.7	n.a.	74.7
Belize	2.7	n.a.	n.a.	n.a.
Bolivia	4.5	4.7	12.0	72.2
Brazil	2.8	3.0	1.4	57.8
Chile	4.4	2.1	4.2	8.2
Colombia	6.0	4.3	–1.7	45.2
Costa Rica	6.8	9.4	–5.0	37.7
Dominican Republic	10.0	3.7	–2.1	n.a.
Ecuador	4.9	3.2	1.3	43.2
El Salvador	3.8	3.9	–4.6	37.6
Guatemala	4.6	4.4	–4.3	17.6
Guyana	1.3	5.3	n.a.	n.a.
Haiti	2.5	11.8	–0.7	n.a.
Honduras	5.6	4.9	–0.2	56.1
Jamaica	2.6	5.8	n.a.	95.2
Mexico	4.8	4.1	–0.3	21.8
Nicaragua	3.7	7.5	–13.6	137.5
Panama	7.5	1.3	–4.2	68.1
Paraguay	4.0	8.9	–3.0	35.9
Peru	7.2	1.5	2.5	37.7
Suriname	6.4	n.a.	n.a.	n.a.
Trinidad and Tobago	12.0	10.0	n.a.	21.6
Uruguay	7.3	6.2	–2.1	70.6
Venezuela	10.0	15.8	17.5	45.9
Latin America and the Caribbean	**5.3**	**4.8**	**1.8**	**45.2**

* 2005.
Note: Average data for current account do not include the following countries: Bahamas, Barbados, Belize, Guyana, Jamaica, Suriname and Trinidad and Tobago. Debt-to-GDP ratio average for Latin America and the Caribbean is not shown, because data are unavailable for some countries.
Sources: GDP, inflation and current account: ECLAC, 2006. Debt-to-GDP ratio: Jaimovich and Panizza, 2006.
n.a.: Not available.

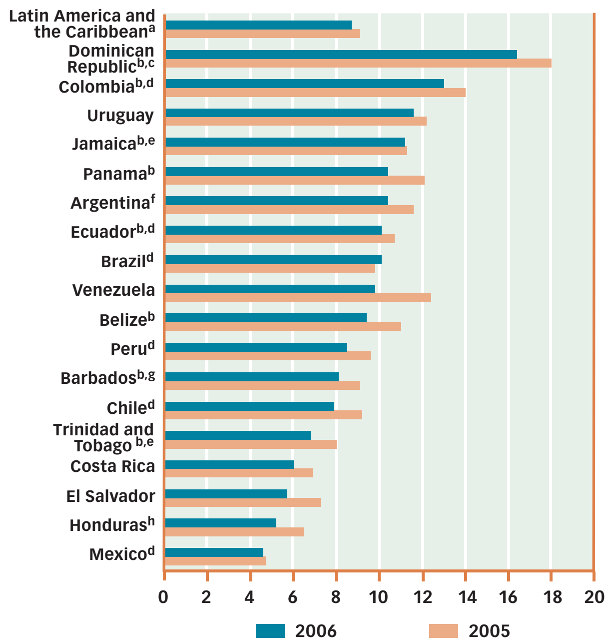
increase (see Figure 4). Labor market rigidities and higher labor participation rates in a few countries have kept unemployment rates from declining further. Job quality remains the number-one concern among Latin Americans.

The poverty level fell below 40 percent of the population in Latin America and the Caribbean for the first time since 1980, with extreme poverty under 15 percent, according to the latest report by the United Nations Economic Commission for Latin America and the Caribbean. Poverty declined from 44 percent to 38.5 percent between 2002 and 2006, and extreme poverty from 19.4 percent to 14.7 percent (see Figure 5).

OUTLOOK FOR 2007

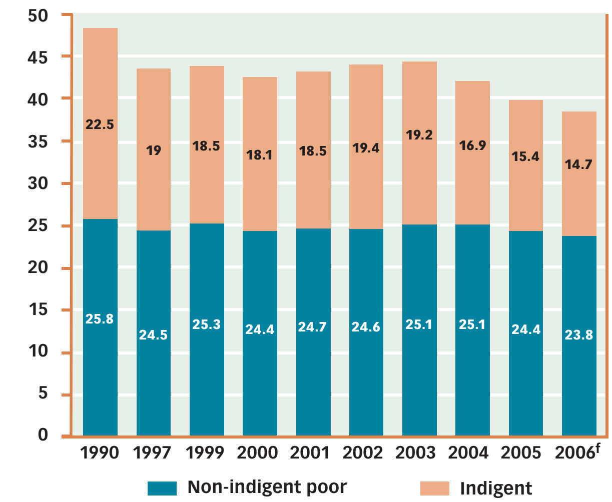
The region's outlook for 2007 hinges on the performance of the U.S. economy, which is showing signs of slowing. While a U.S. recession seems unlikely, it cannot be ruled out. Through its effects on the volumes and prices of Latin American exports, a U.S. recession would translate into at

FIGURE 4. UNEMPLOYMENT, 2005–2006
(Percentage of economically active population)



Source: ECLAC, *Preliminary Overview of the Economies of Latin America and the Caribbean*, 2006.
[a] Preliminary data
[b] Includes hidden unemployment.
[c] Data from April.
[d] Calculations from January to October.
[e] Calculations based on data from January to June.
[f] Estimations based on data from January to September.
[g] Data from March.
[h] Data corresponds to May.

FIGURE 5. POVERTY, 1990–2006
(Percentage of population)



f = Forecast
Source: ECLAC, *Social Panorama of Latin America*, 2005 and 2006.

least two percentage points less growth in the region. As the experience of recent decades has clearly shown, however, the greatest and most unpredictable risks for the region are those originating in the international financial markets. The turbulence of sovereign debt markets midway through 2006 demonstrates how sensitive international financial conditions are.

Barring these critical scenarios, the current outlook suggests 4 to 4.5 percent growth for the region as a whole in 2007. Based on consensus projections by independent analysts, this slowdown will affect nearly all countries, with the possible exceptions of Brazil and Chile. Lower prices for oil and certain other exports may bring the current account surplus down by nearly 1 percent of GDP, but it is expected to remain positive.

The fiscal positions of the majority of countries are also expected to weaken, but without jeopardizing macroeconomic stability. The coming year will be critical for consolidating the sustained growth trends with macroeconomic stability that the region has maintained for several years. The most immediate challenges are to maintain fiscal discipline, strengthen tax collections against future declines in extraordinary tax revenue and improve public debt profiles, as described in Box 1, "Living with Debt."

Most Latin American and Caribbean countries could spur growth by improving their business climate, a task that ranges from making it easier to start a business to enhancing the credibility and efficiency of their court systems. Despite the poverty reduction observed in several countries, it remains a challenge for the region's countries to create quality jobs and expand the reach of social policies targeting the most disadvantaged groups. The success of conditional cash transfer programs clearly shows that innovation and continuity in policies are key ingredients for putting fiscal resources to good use to improve social welfare.

Key Areas

BRAZIL • A commuter train in São Paulo pulls out of the Hebraica-Rebouças station, which was built under a mass transit expansion program.

URUGUAY • Children from at-risk families enjoy playtime as part of an education program.

KEY AREAS

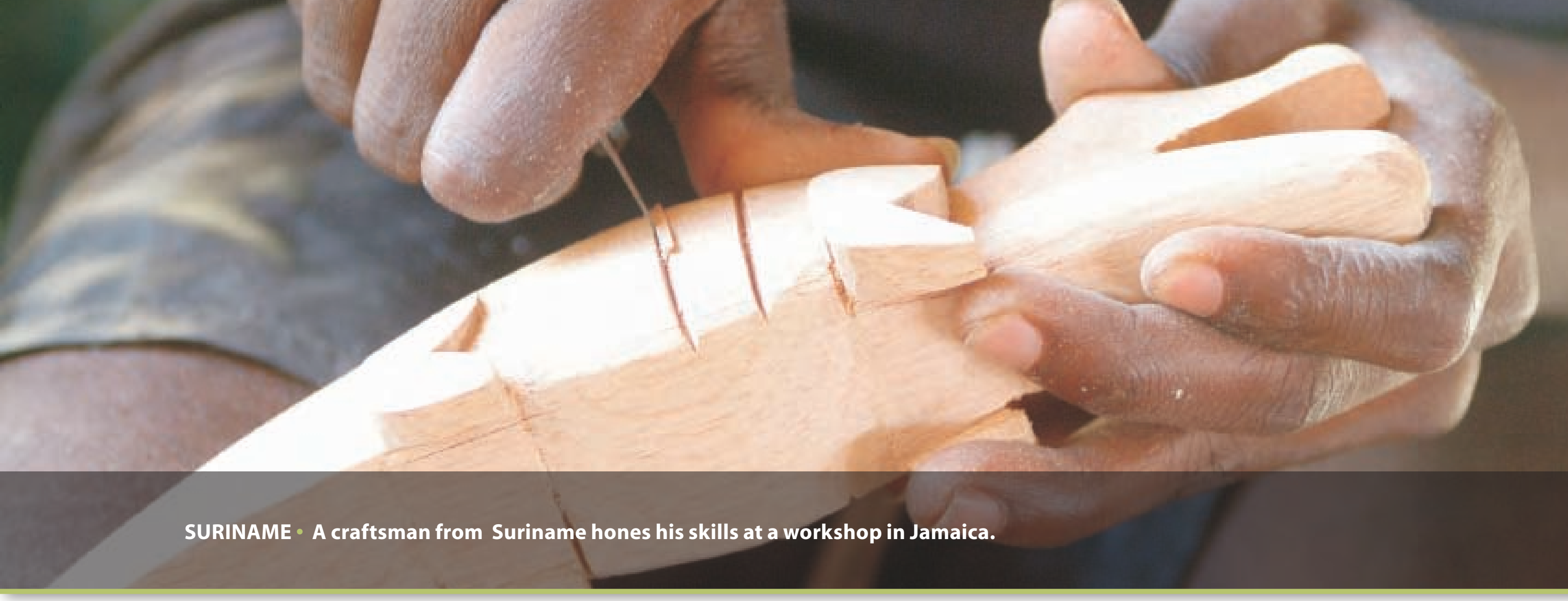
POVERTY REDUCTION AND SOCIAL EQUITY

In 2006 the Bank continued to support poverty reduction and social equity enhancement, its first overarching goal, with 42 operations totaling close to $2.3 billion. These figures represent 37.5 percent of the number of operations and 35.4 percent of the volume of lending, compared with a target of 50 percent and 40 percent, respectively. The cumulative percentage for the 1994-2006 period is 46 percent for the number of projects and 49.3 percent for the volume of lending.

Of the projects approved in 2006, 26 loans for $1.1 billion were specifically designed to reduce poverty. Within this amount, the Bank approved a $27.9 million loan to Honduras and a $30 million loan to Nicaragua to support poverty reduction strategies. In addition, seven loans totaling $370 million were approved for investments in water and sanitation in Ecuador, Haiti, Honduras, Nicaragua, Panama and Uruguay.

Nine other loans for a total of $347 million for infrastructure and productive investments will primarily benefit the poor in Argentina, Bolivia, Guatemala, Haiti, Panama and Peru. The Bank also provided support to strengthen the "Three for One" program for migrants in Mexico, which is an innovative mechanism to channel remittances from migrants into productive local development and social investments, under which the local, regional and central governments each match contributions by hometown associations to development projects.

In December 2006, the IDB's member countries reached an agreement on a framework for debt relief for Bolivia, Guyana, Haiti, Honduras and Nicaragua, the poor-



SURINAME • **A craftsman from Suriname hones his skills at a workshop in Jamaica.**

est countries in the region, in order to assist them in their efforts to achieve the Millennium Development Goals. Under the framework, continuity of the Fund for Special Operations, the Bank's concessional window, and its technical cooperation program for grants will be ensured.

The Bank also continued to increase its knowledge and understanding of the most effective policies for poverty reduction through research, promoting dialogue and improving tools for poverty monitoring. Policy dialogue and knowledge exchange among high-level officials of the region were coordinated at five meetings of the Poverty Reduction and Social Protection Network under the Regional Policy Dialogue. The issues addressed included reaching the Millennium Development Goals, social protection systems, integrated systems for social program beneficiaries, multidimensional poverty measurement, the institutional framework of poverty reduction policies, and access to financial services for the poor.

A trust fund for poverty reduction administered by the Bank was established: the Markets and Governance for Poverty Reduction Trust Fund, with an initial contribution by the United Kingdom of $6.5 million. In addition, the Republic of Korea made a contribution of $19.5 million to the Korea Poverty Reduction Fund, established in 2005. In 2006 the two funds respectively approved 13 projects for $1.2 million and four projects for $1.1 million.

In the area of poverty monitoring, the year 2006 marked the tenth anniversary of the MECOVI program to support the improvement of surveys of living conditions in the region. In commemoration of this anniversary, an international conference was held on "Using Statistics for Broad-Based Development: Challenges for Latin America and the Caribbean," in association with Partnership in Statistics for Development in the 21st Century (PARIS21).

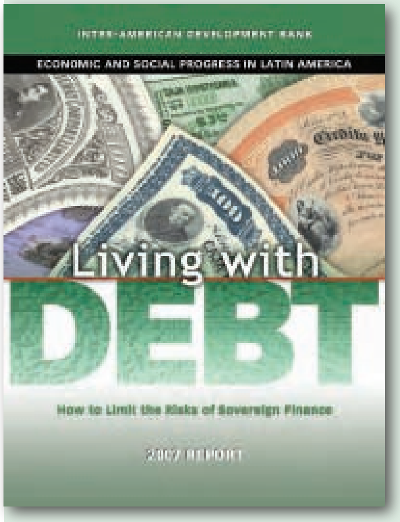
SUSTAINABLE ECONOMIC GROWTH

The second overarching goal of the IDB is to promote sustainable economic growth in Latin America and the Caribbean. For the fourth consecutive year, in 2006 the region posted an average growth rate sufficient to boost per capita income for the population throughout the region. Economic performance was good in almost all the countries, leading to a reduction in poverty. However, governments and analysts remain concerned about the pace of growth in the region. Experts are debating why Latin America and the Caribbean grew 5.3 percent in such a favorable international environment, while other developing regions achieved higher rates.

Argentina and Venezuela have posted high growth rates in recent years, but analysts differ on how sustainable these rates are and on what lessons other countries can learn from the experience of these two nations. Also subject to debate is whether Mexico and the Central American and Caribbean countries should adopt policies that are different from those implemented in South American countries, which are growing at faster rates thanks to the bonanza resulting from high prices of export commodities. Experts are also debating whether South American countries should deliberately support development of new sectors instead of increasing their dependence on the primary sector.

There has been a shift in the conceptual approaches used to analyze problems in growth and to identify priority areas for policymaking. Although analysts have recognized for some time that studies on growth should have a country focus, the traditional approach assumes that growth responds to a combination of factors that are similar in all countries. It uses growth regression to calculate the weight

BOX 1 • LIVING WITH DEBT



The latest edition of the IDB's flagship annual study, the Report on Economic and Social Progress in Latin America and the Caribbean, titled *Living with Debt—How to Limit the Risks of Sovereign Finance*, analyzes the structure and evolution of government debt in Latin America and the Caribbean and the policies that should be followed to reduce the vulnerabilities associated with it. The report recommends that Latin American and Caribbean governments take advantage of the favorable conditions in global markets to adopt safer strategies to manage public sector debt and reduce the risk of financial crises.

Although Latin American debt-to-GDP ratios are not higher than in other regions and spreads of emerging market bonds have reached record low levels in recent months, caution is still in order. "The current relatively benign global environment is partly due to better policies and safer debt management, but it heightens the risk that the international community will become complacent and needed initiatives will be postponed," says the report. "Tranquil times are the best for discussing and introducing new initiatives aimed at reducing the vulnerabilities that still lurk in the global financial system."

Among steps sovereign borrowers could take to address the risk of a sudden stop in capital inflows, the report recommends that countries continue to shift their debt structures away from foreign currency-denominated debt and into debt denominated in their own currencies. Countries should also develop sound domestic bond markets based on a core of institutional investors, such as private pension funds, and consider using contingent foreign currency debt as a mechanism of insurance against adverse shocks caused by recessions, commodity price collapses or natural disasters. Strong fiscal rules and stabilization funds can help build confidence and credibility and at the same time control deficits and establish limits on debt issuance, the report adds.

The study discusses the role international financial institutions could play in improving crisis prevention, such as establishing fast-disbursing liquidity facilities or supporting developing countries' arrangements to pool their foreign currency reserves.

International financial institutions could also promote the development of markets for contingent and local currency financial instruments by including these features in their own bonds and in their loans to member countries.

The report acknowledges that it is proposing a broad agenda that may not win universal support on every single point. But it emphasizes that the risks of inaction are higher than the risks of adopting a reform initiative that is too ambitious. The research for the report focused on the development of domestic bond markets in six Latin American and Caribbean countries. The work was conducted and financed through an IDB-sponsored network of research centers in Latin America.

The book can be ordered from the IDB Bookstore online at **http://shop.iadb.org/iadbstore** and is available in electronic format on the IDB website at **www.iadb.org/res/ipes/2007**.

of these factors and identify the main areas that should be given more attention in analysis and policymaking in each particular country.

In recent years that methodology has been challenged by a new approach that, while not drastically different, is certainly complementary. Developed by Ricardo Hausmann, former chief economist of the IDB, and his colleagues Dani Rodrik and Andrés Velasco, formerly at Harvard University (and currently finance minister of Chile), "growth diagnostics" recognizes that development problems are specific to each country and multidimensional rather than strictly economic in nature. The method identifies the single biggest obstacle to growth in a given country. It is based on information about private and social returns on different factors of production and certain essential inputs (such as infrastructure), along with decisions on the amount and features of investment and production, especially in export-oriented sectors. The findings are charted in a decision tree that analysts use as a road map for country analyses.

Using the new approach, in 2006 the Bank organized a network of research centers throughout the region to study constraints on international competitiveness and growth at the individual country level. Constraints on competitiveness that prevent an increase in public investment are being identified. Teams of researchers will study the cases of Argentina, Chile, Colombia, Ecuador, El Salvador, Guyana, Mexico, Panama, Paraguay and Peru. Soon to be added to the list are Brazil, Guatemala, Jamaica, Nicaragua and Trinidad and Tobago.

The studies will include specific recommendations to the governments and the Bank. The project is expected to contribute to an understanding of the problems the countries must address to accelerate growth through international competitiveness. The studies are being coordinated among the different teams of researchers and take into account similar efforts being carried out by the World Bank and International Monetary Fund.

COLOMBIA • Community outreach workers in Bogotá.

MODERNIZATION OF THE STATE

The Bank's Institutional Strategy establishes four pillars that guide the Bank's work: modernization of the state, competitiveness, social development and integration. In 2006 the Bank approved 25 loans for a total of $1.5 billion and 92 technical cooperation projects for $24.9 million to support modernization of the state, introducing new issues and innovative approaches. The operations covered a broad range of categories, including fiscal, financial and public sector reform; decentralization and development of subnational governments; public safety; civil society participation; administration of justice; e-government; ethics; and planning. Bank resources also supported workshops, seminars, training sessions, publications and other activities to build consensus among all stakeholders.

Subnational development has become increasingly important in national programs for modernization of the state. For instance, a loan approved in 2006 supported subnational management in Chile, the first IDB operation to build capacity systematically in regional and municipal governments using a national system of performance incentives and institutional accreditation. In Brazil, the Bank is launching the PROCIDADES program, a lending

BOX 2 • ONE-STOP JUSTICE IN PERU

In Paucarpata, a working-class suburb of the southern Peruvian city of Arequipa, Cintia Manrique (right) found all the judicial services she needed under one roof instead of having to travel downtown and go from one agency to another.

Judicial systems throughout Latin America have struggled for the past two decades to adapt to the increased demand for judicial services that followed the consolidation of democracy and the concurrent focus on protecting human, political and economic rights. The demand comes from all sides: from companies and entrepreneurs that need to settle disputes quickly in order to compete in liberalized markets; from civil society organizations that are increasingly using the law to hold governments accountable for their actions; and from ordinary citizens who are more willing to go to court to resolve their problems.

Unfortunately, judicial systems are still highly centralized in Latin American countries. Courts and related offices and facilities tend to be located only in large cities, meaning that people who live in rural areas or small towns must make long trips to show up at a hearing. Even within an individual city judicial procedures often require the parties themselves to move paperwork among several government agencies in different locations. And since most judicial proceedings in Latin America are carried out through long series of written submissions—as opposed to oral trials—they tend to be costly and protracted. Lacking the time and the resources to shepherd their case through the system, many people do not use the system at all.

The problem of access has persisted even as the region's judicial systems have embarked on impressive reforms to combat judicial corruption, modernize penal procedure laws and increase the independence and quality of judges. Indeed, many judicial reform experts think that the problem of access—which is closely linked to the quality of judicial administration and management—is the toughest one to solve.

In the 1990s Peruvian authorities decided to tackle the access problem at the ground level. The goal of the Program to Improve Access to Justice was simple: to extend the coverage of the judicial system to marginal areas by offering "one-stop" service centers known as *Módulos Básicos de Justicia* (MBJs, or Basic Justice Modules) that would bring together all the relevant judicial and legal officials under one roof. The program also decentralized the courts by pushing resources and authority out to the MBJs, so that people could obtain a decision and even file a first appeal without having to travel to a central court.

Finally, the program introduced a modern, team-oriented and transparent concept of judicial administration in the MBJs. The goal was to reduce bottlenecks and speed up paperwork by creating "pools" of clerks and administrative personnel that would collaborate on numerous cases rather than work exclusively for a single judge, as in the past.

Diagnostic studies indicated that Peru would need to build around 250 MBJs to provide complete coverage throughout the country. Since the resources necessary to build all these facilities were not available, the government decided on an incremental approach, ultimately building a total of 43 MBJs in high-priority areas between 1998 and 2002. The IDB financed part of the program, lending Peru $11.5 million to help cover construction, equipment and training costs.

According to an evaluation of this initial phase of the program, the MBJs have succeeded in the fundamental goal of bringing justice closer to the public. "In many cases, the MBJs represent the first time the judicial system has been available in large sections of Peru's territory," says the evaluation. "This in and of itself is a historic step forward for justice in Peru." In addition to improving access to the courts, the MBJs are increasing cooperation among the various agencies in the judicial system.

facility administered by the Bank designed to efficiently meet the anticipated heightened demand for municipal loans in a timely manner. Under the facility, project preparation and monitoring activities are concentrated in the country office, for proximity to the client, and specialized agencies or consulting firms are hired to provide services in order to reduce costs associated with the preparation and supervision of projects without compromising their technical quality.

Among its activities to disseminate its Modernization of the State Strategy, the Bank copublished, with MIT Press, a book by Javier Santiso entitled *Latin America's Political Economy of the Possible*, which explains how the economic reforms of the past 15 years have shaped Latin American countries. The Bank also published *The State of State Reform in Latin America*, a comparative study on fiscal and political decentralization in the region since the mid-1980s.

IDB projects have incorporated the Bank's Strategy for Promoting Citizen Participation by introducing components that either contribute directly to building the capacity of civil society organizations or involve them in project execution. Civil society diagnostics and governance issues are also incorporated into overall country strategies, policy dialogue papers and IDB-financed operations.

The Bank has also prepared governance studies for Chile, Colombia, Costa Rica, Ecuador and Nicaragua, addressing both national and subnational issues, as well as operational guidelines for public management in order to strengthen project design in those countries. Through its Regional Technical Cooperation Program, the IDB has disseminated methods to combat corruption and increase transparency in the region, carrying out pilot projects and seminars on such topics as money management and fighting corruption. It has also organized mock trials as a tool to combat money laundering. The Bank is publishing a book on the link between the state, citizenship and development entitled *Justicia: Un vínculo pendiente entre Estado, Ciudadanía y Desarrollo*.

The IDB's increased focus on improving development effectiveness includes helping borrowing member countries build and strengthen their capacity to manage for results and enhancing Bank coordination with other development institutions. A key area is strengthening agencies responsible for the implementation of IDB-financed projects. In 2006, the Bank developed a new Web portal called DataGob (**www.iadb.org/datagob**) that provides a user-friendly interface for accessing more than 280 governance indicators produced by 18 different sources for 32 Latin American and Caribbean countries.

BARBADOS • A worker checks the control panel at a sewerage system that helps sustain water quality.

COMPETITIVENESS

In a globalized economy, competitiveness has become a priority. As development strategies focus increasingly on regional integration, however, experience has shown that

BOX 3 • GENETIC RESEARCH BOOSTS EXPORTS IN CHILE

Genetic research is helping Chilean grape producers stay ahead of the competition.

As one of the world's leading exporters of these products, Chile cannot afford to have table grapes that fall off the vine prematurely or wine grapes whose flavor is spoiled by viruses. The country has long made it a priority to anticipate and combat problems that could compromise quality. Now, in addition to using traditional disease control and selective breeding measures, Chilean scientists are conducting cutting-edge genetic research in an unprecedented effort to develop homegrown solutions to thorny agricultural problems.

The effort is part of an ambitious science and technology initiative launched by the Chilean government in 2001, just as the global revolution in genetic research was beginning to bear fruit. Known as *Chile Innova* ("Chile Innovates"), the Technology Development and Innovation Program grew out of consultations with business groups that have formed partnerships with scientists at Chilean universities. In addition to biotechnology and genetics, the program supports applied research in the areas of information and communication technologies, cleaner production management and quality management of processes and products.

The goal was to focus applied research on areas that can help to make Chile's export industries more competitive. Grapes were a priority for genetic research, since Chile is the world's second-largest exporter of table grapes and the fifth-largest exporter of wine (with wine sales worth approximately $1.2 billion per year). In an effort to improve the quality and yields of grape varieties and to better control vine physiology, Chilean scientists are now conducting genetic research on viruses that affect both table and wine grapes.

The studies have identified genes that determine grape characteristics and measured the effects of various viruses on color, aroma, sugar levels, tannins and resistance to drought and soil salinity. This research has led to the development of prevention systems and diagnostic kits that are used to certify that plants are healthy and free of pathogens.

Thanks to the program, a team at the Universidad de Chile has been able to create three of the most important genetic databases for grape vines in the world. The team has so far identified 60 percent of the grape vine genome and has been able to contribute 24 percent of its newly discovered genes to the global gene pool. Scientists are also in the process of patenting a new research method involving messenger RNA to produce changes in DNA synthesis, a fundamental aspect of genetic research.

The program has also helped private companies understand the business case for investing in research. Chilean scientists and entrepreneurs are forming new partnerships involving plant nurseries, specialized laboratories and companies that are applying genetic research to a growing number of problems within the wine industry. These include vine cultivation and management, fermentation and quality control of the finished product.

Viñas de Chile, an industry association that represents 30 companies that account for 92 percent of the country's wine and grape production, is now planning to contribute $1 million to the genetic research program. And Chile's Association of Fruit Exporters, whose members account for 80 percent of the country's fruit industry, has expressed interest in joining the program in order to benefit other produce, including apples, raspberries, cherries and blueberries (Chile is already the largest exporter of the latter berry in the Southern Hemisphere).

The Technology Development and Innovation Program was supported by a $100 million loan from the IDB. The Bank has played a strategic role in helping to underwrite science and technology initiatives in Chile.

liberalizing trade and entering into trade agreements are not enough to achieve satisfactory performance in exports and to generate the jobs so badly needed in the region. Measures must also be taken to improve competitiveness by attracting foreign direct investment, supporting small business, promoting innovation, deepening cooperation and developing exports.

PARAGUAY • A farming student learns about animal husbandry at a school for rural microentrepreneurs.

During the year, the Bank approved 52 operations totaling $3.2 billion for projects to improve competitiveness in such areas as energy, transportation and communication, trade financing, productive infrastructure, capital markets, agriculture, industry, tourism and science and technology. Approvals in 2006 included a program with a cluster approach to assist rural indigenous communities in Guatemala in developing business services, financing and technical support to make their products and services more competitive.

Competitiveness has improved in only a few countries in the region in recent years. The World Economic Forum's *Global Competitiveness Report* notes that only Argentina, Chile, Colombia and Honduras have moved up by five or more positions in the world ranking of 95 countries according to competitiveness between 2004 and 2006. According to the World Bank's Doing Business system of indicators, in the past two years only Guatemala, Mexico and Peru increased five or more positions in the business environment rankings of 155 countries. Most of the countries in Latin America and the Caribbean dropped in ranking, and overall competitiveness in the region did not change compared with other regions in the world.

In response to this challenge, the IDB has redoubled its efforts to support countries in adopting new policies and improving institutions that can help enhance the business climate and create the right conditions for innovation and investment. A growing number of countries are aware of the need to develop competitiveness strategies, as reflected in the rising demand for projects with Bank support in this area.

The IDB focuses principally on the following types of projects: developing clusters and chains of production to boost local output by strengthening joint action by enterprises, government agencies and civil society organizations; promoting innovation through support for science, technology and innovation; reforming competitiveness policy to strengthen the competitive environment for private companies; providing overall support for competitiveness policies in such areas as business development, financial support for small and medium-sized enterprises and export development; and advancing subnational competitiveness, by strengthening regional development agencies or provincial competitiveness programs that include financial and nonfinancial support for businesses, job training and infrastructure.

In a number of countries, the IDB is providing other support services, such as seminars, grants for technical cooperation and events for dialogue between the public and private sectors on logistics. These are crucial for business competitiveness and act as a link between business competitiveness and economic infrastructure. Competitiveness programs are identified during the programming process with IDB borrowing member countries and are set out in the country strategies.

SOCIAL DEVELOPMENT

The IDB's Social Development Strategy promotes human betterment with special emphasis on reducing poverty and expanding opportunities for the majority. In 2006 the Bank developed the Opportunities for the Majority initiative, which is discussed later in this report. The strategy also addresses the pledge made by the borrowing member countries to work to achieve the Millennium Development Goals, particularly in the areas of poverty reduction, education, health and gender equality.

In 2006 the Bank approved 35 operations for social development totaling $1.7 billion, representing 27 percent of Bank lending. Most of the operations were for social investment programs, followed by water and sanitation, education, health, environmental protection and urban development. The Bank supported health projects in areas where demand has been increasing, such as a regional plan for prevention of an avian and human influenza pandemic, replacement and modernization of infrastructure, developing effective networks to increase coverage and improving the efficiency and quality of health care to reach the needs of the majority.

The strategy also includes assisting countries in reducing social ills, such as crime and violence, which continue to be pervasive, extracting a large cost from the region's economies in terms of forfeited growth. During the year, the Bank continued to expand its innovative portfolio in violence prevention and citizen security, approving operations in Guyana and Panama. Other projects in Costa Rica, the Dominican Republic and Peru are at different stages of development. In addition, the Bank approved grants for technical cooperation to promote decentralization of citizens' security in the region. In a unique partnership with the United Nations Development Programme and the Ricky Martin Foundation, the Bank has worked in a number of countries to combat trafficking in persons.

In 2006, the Bank supported a wide range of initiatives aimed at increasing access to opportunities for disadvantaged people, including those of African descent, indigenous peoples, persons living with disabilities, those living with HIV/AIDS and poor women. During the year the Social Inclusion Trust Fund received replenishment of its initial three-year mandate through a generous contribution from Norway and additional support from Canada, increasing the fund's working capital to nearly $5 million over the next three years. To date, the fund has financed more than $2 million for projects that support emerging programs and policies that address social inclusion in Latin America and the Caribbean.

JAMAICA • A government doctor treats a patient at the St. Jago Park Health Center in Spanish Town.

In the area of urban development, during the year the Bank provided technical assistance to the governments of the province and city of Buenos Aires to improve gover-

BOX 4 • FLAGSHIP MEXICAN PROGRAM LIFTS MILLIONS OUT OF POVERTY

Some 25 million Mexicans benefit from *Oportunidades*, a conditioned cash transfer program that is changing the lives of Mexico's poorest people. Launched in 1997, the program provides aid to indigent families to improve their nutrition and keep their children healthy and in school. Its quick and encouraging results led the IDB to approve a $1 billion loan in 2002—one of the largest investment loans in the Bank's history. A second loan for $1.2 billion was approved in 2005.

A young mother receives her bimonthly Oportunidades payment from a bank official in Veracruz.

The program has several features that distinguish it from previous poverty reduction initiatives. Aid is delivered in cash rather than in kind, and is given directly to the female head of household. Payments continue to flow as long as beneficiaries meet a series of conditions, namely, keeping their children in school, taking them to see a doctor regularly and getting their shots, and attending periodic discussions on topics such as health, nutrition, hygiene, domestic violence and family planning. Pregnant women, lactating mothers and babies are also provided an iron- and micronutrient-fortified formula that helps prevent infant malnutrition.

The program has grown from 300,000 families in 1997 to 5 million in 2004, covering virtually the entire population threatened by hunger. The closely monitored and meticulously evaluated initiative has quickly shown impressive improvements in beneficiary families' food consumption, infant weight and height growth, use of preventive medical services, prenatal care and contraception, school enrollment and retention and a reduction of the incidence of child labor.

Beyond statistics, *Oportunidades* has empowered women by trusting them to manage money for their families. Through the program, mothers who never went to school or dropped out after one or two grades are signing up for adult education. Around 1.2 million families receive their bimonthly stipends in bank accounts created by *Oportunidades*. Some families have even started to build up savings, as mothers and fathers salt away a few pesos they would have otherwise spent or stuffed under a mattress. The program's education subsidies also cover high school. As a further incentive for students to graduate, it now contributes to individual savings accounts that help its young beneficiaries accumulate some money to pay for higher education, start a small business or buy a home.

Several firewalls guard against abuse, political manipulation and corruption. For instance, the stipends have ceilings (no family can receive more than $150 a month) so there is no reward for having more and more children. *Oportunidades* staff do not handle money. The tasks of stuffing, sorting and delivering cash envelopes to beneficiaries are outsourced to commercial banks, a state-owned bank and the telegraph company. Prior to elections there are "blackout periods" during which no payments may be made and no families may be added to the roster.

Another distinguishing feature of the program is its low operating costs. With a core staff of around 630 people, *Oportunidades* spends only about 5 cents out of every peso on administrative expenses. Up to 12,000 people are employed as temporary workers to conduct house-by-house surveys and to input data during enrollment periods. Part of the clerical work is done by university students who must meet a required number of hours of social work before they graduate.

But perhaps the program's most salient characteristic is that evaluations have played a key role from the start. Its deliberately gradual growth allowed its administrators to gauge what worked and what needed fine-tuning. The International Food Policy Research Institute reviewed the program in 2001 and found that after just three years, Mexican children from poor families in rural communities covered by the program were attending school for longer periods, eating more balanced diets, receiving medical care more frequently "and learning that the future can be very different from the past."

The program's success moved the IDB to encourage other Latin American countries to study the Mexican model and adapt it to their particular needs. Argentina, Brazil, Colombia, Ecuador, El Salvador, Honduras, Nicaragua and Peru are among the countries that have drawn from Mexico's experience in their implementation of social programs in education, health and nutrition.

COSTA RICA • **The Angostura 177-MW hydroelectric power plant is the centerpiece of a project to expand coverage, maintain quality and conserve energy.**

nance, on selected problems affecting the Buenos Aires metropolitan area. It also published a book, entitled *Gobernar las metrópolis*, which surveys the democratic and fiscal principles of good metropolitan area governance and current practices around the world.

In 2006 the Bank approved 18 lending operations, 20 percent of all loans approved, for $541.6 million, that included specific actions to promote gender equality or women's participation. Also, 62 nonreimbursable technical cooperation projects, totaling $15.5 million, supported initiatives that incorporate a focus on gender issues, including 21 (totaling $2 million) that established as their primary objective promoting gender equality or addressing priority issues for women.

During the year, the Gender Mainstreaming Trust Fund started operations with an initial contribution from the government of Norway for $3 million, financing 17 small technical cooperation projects to support gender mainstreaming for a total of $625,000. For example, the fund supported a gender assessment of housing in Honduras to integrate gender issues into a loan for a low-income housing program that will guarantee equal access to property ownership and title for women by requiring that titles be issued in the woman's name or jointly with her spouse's name.

In 2006, three loans specifically targeted at indigenous peoples were approved, including a $45.2 million loan for the second phase of the Chile Integrated Development for Indigenous Peoples program for rural Mapuche, Atacameño and Aymara communities. In addition to these operations specifically designed to benefit indigenous peoples, another 19 loans had specific components, targeting or impact mitigation measures for indigenous people.

During the year, a record 37 technical cooperation projects were approved specifically addressing indigenous issues, reflecting the growing awareness and demand on the part of governments and indigenous peoples in the region. The increase may also reflect the impact of the consultations and discussions surrounding the Bank's new indigenous policy and strategy.

In February 2006, the Board of Executive Directors approved an Operational Policy on Indigenous Peoples and a Strategy for Indigenous Development, along with guidelines to implement the policy. The strategy emphasizes support for the mobilization of the potential of indigenous peoples for culturally relevant economic development based on their considerable natural resources, social capital and cultural heritage, and responding to niche markets where indigenous peoples have comparative advantages.

INDES

The Bank's Inter-American Institute for Social Development (INDES) is a pioneer in social management training, offering a series of courses, workshops and seminars to enhance the skills of leaders and administrators in government and nongovernmental organizations in developing and carrying out social policies and programs to achieve greater efficiency and equity.

In 2006, INDES held 12 regional training sessions to enhance the skills of more than 300 professionals—41 percent of them women—in areas such as health, education and other basic social services.

BOX 5 • BRIDGING THE LAST FRONTIER IN SOUTH AMERICA

The new Acre River bridge links Brazil with Peru and the west coast of South America.

A person traveling from Rio Branco, capital of Brazil's westernmost state of Acre, toward the little town of Assis on the border with Peru is not merely driving along highway BR-317. As a big overhead sign proclaims on the approach to Assis, this is the *Estrada do Pacífico*, the Road to the Pacific, the realization of Brazil's long-standing dream of an outlet to west coast ports. In about a year's time, completion of the Peruvian segment of the Road to the Pacific will enable South American travelers to drive paved roads from the Atlantic to the Pacific.

The inauguration in January 2006 of a new bridge over the muddy Acre River, which divides Brazil and Peru, transformed Assis from one of the most isolated communities in Brazil into a pivotal node in a vast network of transportation, energy and telecommunications infrastructure projects. This network is IIRSA, the Spanish acronym for an initiative known in English as the Integration of Regional Infrastructure in South America. IIRSA's thick portfolio of projects (335 in all) includes 31 accorded top priority—bridges, roads, railroads, waterways and gas pipelines. Many are already under construction, and most should be completed by the 2010 deadline.

On the other side of the bridge, heading west from the Peruvian border town of Iñapari, the road quickly turns to dirt. Dusty and punishing to both drivers and shock absorbers during the area's few months of dry weather, the road becomes a muddy morass during the 10-month-long rainy season, turning the 740-kilometer drive to the Andean city of Cusco into an exhausting weeklong ordeal.

Roads such as this one, common throughout the interior of South America, pose particular problems for producers and shippers. Completion of the Road to the Pacific is therefore expected to unleash the economic potential of Brazil's vast interior, including the Amazon Basin, providing producers with a cost-effective way to ship soy, timber, cattle and other products to Asian markets and opening up ample opportunities for business, transport, finance and job creation in currently isolated areas. There is also the prospect of increased cross-border tourism. For example, easier access offered by the Road to the Pacific may make it more inviting for the million tourists annually who travel to the Inca capital of Cusco and the ruins of Machu Picchu to visit the Brazilian Amazon.

Thus, paving the Peruvian segment may be a higher priority for Brazil than for Peru: Brazil's development bank, BNDES, has lent $417 million to Peru to complete the project. The Andean Development Corporation is lending an additional $300 million, and the Peruvian government is investing $100 million.

IIRSA's Technical Coordination Committee, composed of the IDB, the Andean Development Corporation and FONPLATA, a regional agency that funds projects in the River Plate basin, provides technical and financial support for the initiative. The IDB has a $20 million fund for technical cooperation to support regional integration initiatives in Latin America and the Caribbean such as IIRSA. The fund may be used to finance prefeasibility and feasibility studies, project design, environmental studies and other activities to prepare infrastructure projects in the priority areas identified by IIRSA and other initiatives.

BOX 6 • CENTRAL AMERICAN ENERGY

In response to requests from Central American countries to help mitigate the impact of high oil prices, the IDB joined other regional institutions that participate in the Central American Integration System to forge a plan for energy integration and development. Later expanded to the Dominican Republic, the plan identified short-term priority measures for energy efficiency and diversification, renewable energy, and, more specifically, the development of biofuels.

During the year, the IDB provided support for a series of technical assistance projects in conjunction with the Central American countries, the Dominican Republic, Mexico and Colombia. Among these projects are sustainable small hydropower plants in Central America, energy efficiency in Nicaragua and feasibility studies on biofuel programs for Mexico and El Salvador.

Regional meetings were held on energy efficiency and renewable energy, and a Mesoamerican Biofuels Working Group was established to prepare a regional action plan. A regional carbon credit project portfolio was developed to attract public and private investments in renewable energy and energy efficiency. Regional programs were prepared on efficient lighting in residential and commercial spaces in the services industry, energy efficiency in water pumping systems and low-investment measures for increasing efficiency in urban transportation, along with a Regional Action Plan for Geothermal Energy, which also

received support from the Japan Bank for International Cooperation.

In response to the Mesoamerican Energy Integration Program endorsed by the heads of state of Central America, the Dominican Republic, Mexico and Colombia, the Bank funded feasibility studies for two major energy projects in Central America: construction of an oil refinery for crude oil from Mexico and the introduction of natural gas in the region.

The Bank continued its support for increased rural electricity coverage in Central America with an innovative loan to Panama using sustainable renewable energy solutions; ongoing implementation of the Central American Interconnection System; and studies for a future Panama-Colombia electric interconnection.

Through its national programs, INDES trained approximately 450 individuals at 22 sessions during the year. The institute also carried out four three-day seminars for managers in the region, training more than 400 professionals. INDES expanded its distance learning courses, offering 12 online programs for 700 social program managers, 54 percent of them women. Many of the participants were from areas outside the capital cities.

INTEGRATION

The Bank continued providing extensive support to countries in the area of regional integration, one of the four pillars of its Institutional Strategy. Key efforts involved multitiered support for the various subregional, hemispheric, interregional and multilateral integration initiatives through loans, national and regional technical cooperation, training, seminars and workshops, research publications, and policy papers.

A wide range of operations was approved during 2006 to assist the region collectively and countries individually in expanding opportunities for regional and global integration. The Bank continued its strong support for subregional integration, approving 20 regional technical cooperation projects. Support for integration in the Southern Cone focused on technical work aimed at implementing the MERCOSUR Regional Strategy and a technical cooperation project to facilitate cooperation in sanitary standards.

CHILE • Customs procedures were streamlined under a modernization program.

The Bank funded a regional technical cooperation operation in the Andean Community for the administration and verification of rules of origin regimes, and copublished a book on fiscal equity with the Community's General Secretariat.

Support for Central America included projects for implementation of the Central America–Dominican Republic–United States Free Trade Agreement (DR-CAFTA) in regard to intellectual property rights and labor issues; compliance with labor regulations; infrastructure projects under the Puebla-Panama Plan; consolidation of the customs union; and preparation for the Association Agreement negotiations with the European Union that are scheduled to commence in early 2007. Jointly with the International Monetary Fund, the Bank provided technical support to the six Latin American DR-CAFTA members and Panama on international taxation and harmonization issues.

Bank support for Caribbean Community integration during the year included five regional technical cooperation projects in areas such as harmonizing regional quality infrastructure, strengthening public outreach and monitoring mechanisms under the Caribbean Single Market and Economy. The Bank also provided support to Guyana for coordination and consensus building in its role as chair of the Rio Group.

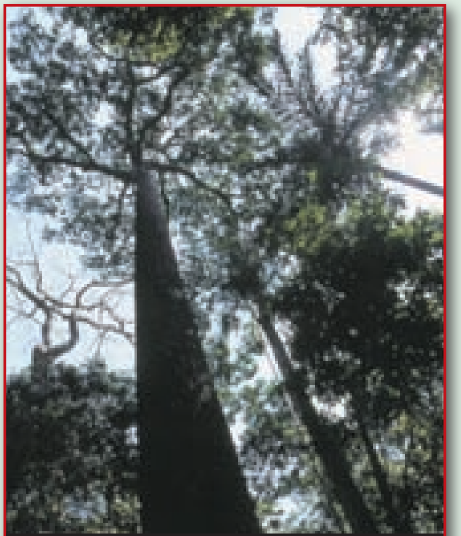
In addition, four loans approved during the year included integration-related components: programs for competitiveness in Colombia and Guyana, fiscal reform in Bolivia (customs and tax harmonization components), and public financial management in Honduras (customs component). Eight of the Bank's flagship national technical cooperation projects were trade-related, centering on such areas as strengthening investment promotion in Haiti, enhancing competitiveness in the textile and apparel industries in Honduras and Guatemala (with financing from the Multilateral Investment Fund), and studies on trade-related tax reform in the Dominican Republic (Korea Fund).

As a part of its Integration Strategy, the Bank continued promoting the creation of regional public goods in 2006, approving 11 new projects for $9.7 million; the projects benefit the 26 borrowing member countries across seven different sectors. During the year, nine hemispheric meetings and 13 subregional ones were held for the Regional Policy Dialogue networks—Education, Natural Disasters, Environment, Trade and Integration, Public Management and Transparency, Poverty, and Central Banks and Finance Ministries. A new Science, Technology and Innovation Network will be launched in 2007.

The IDB also embarked on a major pioneering initiative to examine the links between trade and poverty—the social impact of trade liberalization—and how to make trade policy a tool for poverty reduction in Latin America

BOX 7 • BRAZILIAN RUBBER TAPPERS PRESERVE THE RAIN FOREST

For generations, rubber tappers in the São Luís do Remanso extractive reserve in western Brazil have made their living by tapping rubber trees and gathering other natural products, such as Brazil nuts. It's a meager life in which options are few and hard times are always waiting around the corner.



A carefully managed forest can protect biodiversity even as it produces profits.

When experts from the Center for Amazonian Workers (CTA, after its name in Portuguese) proposed that the tappers could make a living by cutting trees from the forest and selling them—in a way that would have little long-term impact on the forest—the people were interested but skeptical. While they understood the forest, they knew nothing about forest management: making inventories of trees, creating maps, designing cutting schedules, calculating income and costs and profits, planning capital investments and navigating regulatory red tape. It took nearly two years of meeting with CTA experts before the tappers became convinced that forest management was their future.

Community-based management of São Luís seemed, in fact, to be part of the forest's destiny. The forest's very existence is owed to Chico Mendes, an internationally revered defender of the rights of local people killed in 1988—the same year the reserve was created—by powerful interests who wanted to take over the rubber tappers' forests. By extracting more benefits from the reserve while continuing to protect it, the tappers would be honoring their fallen hero.

The forest itself is rich not only biologically, but economically, with the impressive species diversity of tropical rain forests and a particular abundance of valuable mahogany and Spanish cedar. A well-designed management plan could therefore reconcile to a certain extent the competing aims of conservation and business by harvesting many different trees—including trees that had not previously been considered marketable—to maintain the existing species composition. Finally, the reserve is close to good transportation as well as to processing firms in the nearby state capital of Rio Branco.

Some 30 families in São Luís do Remanso are now managing forest parcels using skills they learned from courses given by experts from the CTA, whose work is being financed with the help of a $750,000 grant from a fund that the IDB manages on behalf of the government of Japan. Of these families, 10 are engaged in managed forestry. The others collect and sell other forest products, such as oil from the copaiba tree and seeds, and produce handicrafts.

The management area in São Luís is formed by five family-owned forest parcels. Under the management plan, only a given number of families harvest trees each year. The total area exploited is large enough to allow skidders (tractors used for hauling logs) and trucks to do their job efficiently and with minimum collateral damage to the forest.

Each year's harvest includes both high-value hardwoods and lower-value "white" woods that are used for plywood. Part of the year's profit is for working capital for the community management organization; another part is earmarked to build up social funds for eventual projects in education, health, training and other areas. The remainder is distributed to the families, in accordance with the labor they have invested and their level of production. The hope is that the forest will continue to provide biological and economic benefits for many generations to come.

and the Caribbean. Some of the analytical work is being financed by the Bank's new Trade and Poverty Trust Fund, launched in 2006 with funding from the Department for International Development of the United Kingdom. The fund has five technical cooperation projects in execution and more than a dozen in the pipeline.

The Bank also continued working on various cross-cutting training initiatives and analytical products in support of integration and trade. Training centered on verification of rules of origin, and on uses of Computable General Equilibrium Model assessments of trade liberalization scenarios; two sets of software aimed at helping trade negotiators simulate the effects of different trade negotiations scenarios were enhanced. Some of the key outputs included research on sequencing of integration; the relationship between regional integration and regional cooperation; options for Latin America and the Caribbean in the Doha Development Agenda; and mechanisms to diversify exports. Reflecting the Bank's long-standing analytical attention to the effects of the Asian economies on Latin America, the Bank published, with Harvard University Press, the acclaimed volume *The Emergence of China: Opportunities and Challenges for Latin America and the Caribbean,* which provides an in-depth analysis of measures to further Latin America's competitiveness and leverage its competitive advantages in light of the rise of Asia on the global economic stage.

The Bank also continued a variety of activities with the Latin American/Caribbean–East Asia Economic and Business Association (LAEBA), jointly with the Asian Development Bank Institute, including cohosting the LAEBA 2006 annual meeting in Seoul, and solidified its extensive cooperation with the World Trade Organization, Asian Development Bank, Organisation for Economic Co-operation and Development, United Nations and other organizations on trade and integration issues.

INTAL

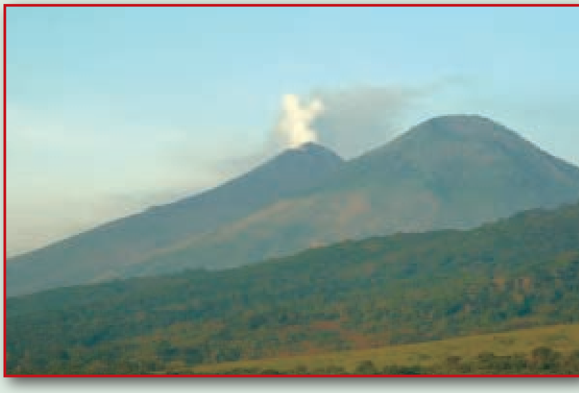
The Bank's Institute for the Integration of Latin America and the Caribbean promotes Latin American and Caribbean integration at the subregional, regional, interregional, hemispheric and international levels through research, technical assistance and training. In 2006 it continued its extensive training program with the World Trade Organization to strengthen countries' trade negotiation capacity and supported policy research networks, including LAEBA, the Euro-Latin Study Network on Integration and Trade, and the Integration Research Centers Network.

OPPORTUNITIES FOR THE MAJORITY

A number of Bank activities encompass more than one of the four pillars described above. During the year, the Bank also launched its Opportunities for the Majority initiative, which concentrates on bringing the benefits of economic

SURINAME • The Low-Income Shelter Program is helping to finance the construction of 1,000 new homes.

BOX 8 • PREVENTING LOSSES FROM NATURAL DISASTERS



Hurricanes, earthquakes, landslides and floods cause $3.2 billion in physical losses each year, on average, in Latin America and the Caribbean. Natural disasters in the region claim more than 5,000 lives annually and affect four million people. Mitigating the risk associated with natural disasters involves both practical measures that will reduce vulnerability to loss of life and property when disasters strike and steps to soften the impact of disasters on countries' economies.

During the year, the Bank established a $10 million Disaster Prevention Fund to support disaster risk management activities and preparation of disaster prevention projects. The fund's first operation was approved in December, a grant to Colombia for preparation of a strategic action plan to mitigate the risks facing the population living in highly vulnerable areas near the Galeras volcano. A complementary multidonor disaster prevention trust fund was also established in 2006, with expressions of support from Japan, the Republic of Korea and Spain.

In the case of Guatemala, the country faces an ongoing challenge in its recovery from devastation sustained in 2005 as result of torrential rains and Hurricane Stan. Not only must it rebuild, but it must rebuild more safely, strengthening critical infrastructure against future floods, and locating investments in low-risk areas. Two Bank-financed programs are helping Guatemala lay the groundwork for better and sustained risk management well into the future.

The first program promotes safe reconstruction practices through Bank-financed communication and knowledge management support in affected municipalities. Under this program, communities in five departments most affected by the hurricane have access to technical know-how, helping ensure that reducing vulnerability remains a priority throughout the reconstruction period, which is likely to last well into 2007.

The second program is helping Guatemala take the first steps towards integrated risk management in the public sector. With Bank financing, critical risk information is being improved and criteria for planning investment and recurrent expenditures are being revised, in view of the sizable contingent fiscal liability the country faces as a result of earthquakes and hurricanes.

Countries wishing to mitigate the financial risk associated with national disasters, as Guatemala is doing, must have access to accurate information about probable losses from natural hazards. Across Latin America and the Caribbean, this type of information has not been readily available. To address this gap and to provide decision-makers with risk information that can be easily interpreted and acted upon, the Bank is supporting two important initiatives.

The first is a system of indicators that depicts disaster risk at the national level and helps identify developmental and technical assistance needs for strengthening country risk management systems. This system, which drew on two decades of data from 12 Latin American and Caribbean nations, was expanded in 2006 with data on two additional countries, Bolivia and Nicaragua. The second initiative, undertaken in 2006, evaluates probable losses due to earthquakes and hurricanes in high-risk countries in the region using formal catastrophe modeling. Evaluations based on such modeling are currently underway for Bolivia, Guatemala, Jamaica and Peru.

In recognition of its commitment to a proactive disaster risk management approach in Latin America and the Caribbean, the IDB received the 2006 Silent Defender Award from the International Code Council Foundation. This annual award honors individuals and institutions that are dedicated to mitigating the impacts of natural disasters and other tragedies by promoting the construction of durable, safe buildings.

growth and knowledge to the majority in the region, that 70 percent of the population comprising 360 million people with annual earnings of $3,260 or less. Rather than approaching the issue from a macroeconomic perspective, the initiative views it through a microeconomic lens, engaging the business community, governments and civil society in addressing the needs of the majority.

The initiative focuses on empowering the majority to participate effectively in economic life, recognizing their potential as both producers and consumers. Programs and projects designed to improve the living and working conditions of the majority that meet specific targets and have a substantial, measurable development impact will be central to the initiative. The private sector and other stakeholders will be engaged in developing innovative pilot projects, undertaking research and formulating proposals to reengineer processes, remove obstacles and harness markets to create opportunities for the majority.

The initiative concentrates on six strategic areas of activity targeted for their potential to directly generate inclusive growth for the majority and produce measurable results in the five-year period from 2007 to 2011: citizen identification, financial democracy, job creation and entrepreneurship, basic infrastructure services, information and communication technology, and housing. Work in these areas will be supported by the Atlas of the Majority, an interactive web-based tool that compiles relevant indicators on economic participation and the living conditions of the majority in the region (**www.iadb.org/om**).

The IDB is developing an Innovation and Opportunity Network to identify, analyze and test new partnerships with all levels of government, the private sector and civil society. The Bank will incorporate into its lending new research and lessons learned from pilot projects. Subregional centers will be competitively selected across the region to be part of the network, which will operate initially for a five-year period.

The goals of the Opportunities for the Majority initiative are ambitious, based on a view that no single entity alone can address the challenges for the region. Inviting multiple stakeholders to join in the Bank's development efforts will bring new ideas, further the Bank's strategy of working in partnership with the private sector and create synergies that will enable all the various participants to see problems and challenges in a new way. Such cooperation will lead to previously unimagined or undeveloped solutions that will be more effective in addressing the region's goals.

ENVIRONMENT

In January 2006 the Board of Executive Directors approved the Environment and Safeguards Compliance Policy, which entered into effect in July. The new policy consolidates current IDB practices and aligns them with sound environmental practices of other multilateral development institutions,

PERU • A diver harvests scallops in Paracas Bay, where a pollution abatement project has restored the sea harvest.

BOX 9 • THE SUSTAINABLE ENERGY AND CLIMATE CHANGE INITIATIVE

As energy demands in the region continue to grow, with energy prices rising and the reliability of the energy supply still an issue, ensuring affordable and reliable sources of energy remains at the core of the development agenda for Latin America and the Caribbean. In addition, the impacts of uncontrolled climate change threaten to undermine the region's economic and social well-being, increasing its vulnerability to climate risks such as natural disasters, disruptions of agriculture and loss of biodiversity. A recent Bank study calculated that a quarter of Bank-financed projects could be at risk from climate change.

Sugar cane, grown in several Latin American countries, produces the most efficient biofuel.

The Bank's Sustainable Energy and Climate Change Initiative aims to support the region in finding economically and environmentally sound energy options. Its core objectives are to expand the development and use of renewable energy sources, energy efficient technologies and practices, and carbon finance in the region, as well as to promote and finance climate change adaptation strategies that reduce the region's climate vulnerability.

The initiative is built around four pillars, designed to help the Bank and the region achieve energy sustainability objectives.

The first pillar involves renewable energy and energy efficiency, with an emphasis on meeting energy needs identified during country programming and strategy development through renewable energy and energy efficient technologies. The Bank is encouraging the development of new projects that incorporate these sources and technologies, as well as examining existing projects to identify opportunities for promoting these goals. A key component is Bank support for minimizing regulatory, institutional and financial barriers and establishing incentives for pursuing goals in this area.

Biofuel development is the goal of the initiative's second pillar. The Bank plans to provide country-level policy assistance in support of biofuel development. Lending is being made available for biofuel programs, including feedstock development, biofuel production facilities and related infrastructure. Financing is also being provided for the adaptation of new and emerging biofuel technologies that have been proven effective.

The third pillar focuses on ways of increasing access to carbon finance in the region. Under the Kyoto Protocol to reduce greenhouse gas emissions, "carbon credits" earned by those who have reduced their carbon outputs below targeted levels can be "sold" to those whose total carbon output still exceeds their emissions cap under the protocol. As the IDB seeks to bring carbon finance into the mainstream of its operations, it is developing projects under the protocol's Clean Development Mechanism (a means of earning carbon credits). The Bank is also aiming to lower transaction costs and risks for project development in this area.

The fourth pillar of the initiative, adaptation to climate change, seeks to incorporate the assessment and mitigation of climate risk in country programming (through the financing of risk and vulnerability assessments and identification of adaptation measures) and to make IDB investments "climate-proof." The idea is to reduce the vulnerability of urban and regional infrastructure to climate risk.

IDB President Luis Alberto Moreno launched the initiative in November at a meeting of government officials and experts at Bank Headquarters to discuss challenges and opportunities to increase investments in sustainable energy in the region. During the two-day conference, these leaders debated strategies for energy efficiency and carbon finance issues, analyzed ways to support the development of biofuels and carbon finance markets, and looked at current experiences in the private and public sectors, in areas such as housing, transportation and rural electrification.

as well as with the Equator Principles, a financial industry framework for addressing environmental and social risks in project financing that has been adopted by numerous commercial banks.

The policy applies to all public and private operations of the Bank. It prescribes a set of directives and safeguards that will be incorporated into the mainstream of IDB operations and procedures, enabling the Bank to shift emphasis from impact assessment to a more strategic risk management approach. The policy is accompanied by guidelines approved by IDB management that provide Bank staff and executing agencies with specific procedures to assist them in proper implementation and compliance with the policy. As part of policy implementation, a comprehensive training and skill development program for all Bank staff will take place in 2007 and 2008.

DOMINICAN REPUBLIC • Puerto Haina was improved and expanded to accommodate bigger ships, thereby increasing international trade.

In the area of operations, a total of 19 environment loans for $538 million were approved in 2006, primarily in the areas of water and sanitation, disaster risk management, integrated natural resource management and sustainable tourism. In addition, a total of 82 technical cooperation grants totaling $19.8 million for environmental projects were approved in such areas as integrated natural resource management, water and sanitation, environmental policy and institutions, urban environmental management and pollution abatement, sustainable agriculture and coastal management. For example, lending to The Bahamas included support for coastal zone management and natural disaster preparedness.

With many new environmental projects in the pipeline, the lending portfolio is expected to expand considerably during 2007. New projects will cover areas such as sustainable tourism and agriculture, integrated urban environmental development and biodiversity conservation.

INFRASTRUCTURE

The quality, price and coverage of electricity, gas, water and sanitation, telecommunications and transportation are decisive factors in a country's success at improving the well-being of its population and becoming competitive in an increasingly globalized world. In 2006, the IDB continued its sustained effort to support infrastructure development, approving 21 projects for a total IDB contribution of $1.8 billion, including 16 public sector projects ($1.4 billion) and five private sector projects ($347 million). From 1995 to 2006, the IDB provided $16.7 billion in financing for 225 infrastructure projects.

The Infrastructure Investment Fund (InfraFund) was launched by the IDB during 2006 as a vehicle to support the preparation and development of sustainable projects in Latin America and the Caribbean. The $20 million fund will foster the development of critical infrastructure projects in the region. The Bank plans to lend $12 billion for such projects over the next five years.

The Multilateral Investment Fund (MIF) has played an important role in encouraging private sector participation in infrastructure. During the year the MIF approved six grants totaling $4 million for such projects. Since its incep-

PANAMA • Colonial ruins near Panama City. Tourists can enjoy more modern, efficient and environmentally sustainable facilities under a tourism sector investment program.

tion in 1994, the MIF has made more than 106 grants for over $89.7 million to bolster the reform process, including operations to modernize the legal and regulatory systems, privatize utilities, strengthen institutions and restructure economic sectors.

Among the most recent infrastructure operations is a $61.3 million loan for a water supply and sanitation program in Cuenca, Ecuador. Designed to meet demand on a sustainable basis for the third-largest city in the country, the program targets the population that currently has unreliable service. Good-quality services will reduce the risk of waterborne diseases, prevent deterioration of water quality in rivers running through Cuenca by ensuring proper disposal of wastewater and help reduce the risk of flooding in the city during periods of heavy rainfall. The IDB took several steps in 2006 to help the countries of Latin America and the Caribbean set priorities for improved water and sanitation services and arrange financing and technical assistance.

With the expansion of authority for lending without a sovereign guarantee, the IDB now has greater flexibility to tailor financing terms to the specific needs and risks of public water companies. The Bank is preparing to launch a new water initiative consonant with the needs and capacities in the region. To this end, the Bank approved some $370 million for water projects in 2006 and has already identified 19 projects totaling $1.1 billion for the 2007–2008 project pipeline.

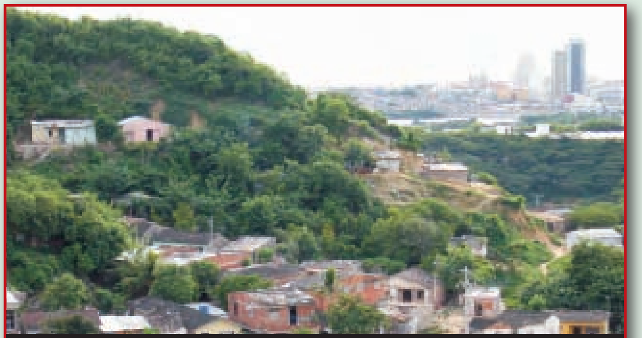
PRIVATE SECTOR DEVELOPMENT

The Bank expanded its capacity to lend to private sector and subnational entities during 2006. A new business model, approved by the Board of Governors at the Annual Meeting in Belo Horizonte, Brazil, and implemented through operational guidelines and a business plan approved by the Board of Executive Directors in August 2006, provides for lending without sovereign guarantees to private, state-owned and mixed-capital companies. Under the new model, the IDB can lend directly to financial institutions, as well as companies active in all sectors, including oil and gas, agribusiness, mining, manufacturing, tourism, technology and services.

The new model allows the Bank to meet the growing demand for credit among subnational entities, which have been strengthened by the decentralization that has been widely adopted in Latin America in the past two decades. Many of these municipal and provincial governments are now actively seeking financing for projects to improve basic infrastructure in areas such as water, sanitation, electricity, roads and transportation, often in partnership with the private sector.

These changes cap a year-long overhaul of the IDB’s policies intended to make the Bank a more agile and responsive partner to governments, private companies and public-private ventures throughout the region. Recent

BOX 10 • WATER RUNS UPHILL IN COLOMBIA



Until 2002, people in this part of Cartagena depended on water delivered on donkeys' backs.

Until a few years ago, the *burroducto* was the only source of potable water for tens of thousands of people who live on steep hills overlooking the historic Caribbean city of Cartagena. Informal vendors filled large cans from taps in the lower part of the city, strapped them to the backs of burros, then guided the animals up dirt tracks and eroded gullies to the shantytowns, where they sold the water for many times what it cost in the rich beachfront neighborhoods connected to Cartagena's municipal water service.

Today, thanks to a public-private partnership that now provides Cartagena's water service, residents of the hill communities have access to potable water that flows 24 hours a day—for about a fifth of what they were paying for the *burroducto* water.

What makes the success of Cartagena's "mixed-capital" water provider, ACUACAR, so remarkable is that since the more affluent areas of the city already had decent water service when ACUACAR began operations, virtually all of its activities have been focused on Cartagena's low-income areas. And in contrast to the strong public opposition that has greeted private investment in the water sector in some other parts of Latin America, Cartagena's public-private water company enjoys broad public support.

Cartagena has succeeded where so many other cities have not, thanks in part to an innovative Colombian government strategy that emphasizes local autonomy, clear objectives, financial self-sufficiency and flexible use of both public and private management models. A series of legal and constitutional changes in Colombia in the 1980s gradually transferred responsibility for water and sanitation from central to local governments, letting municipalities decide how these services should be organized (including whether to allow private investment).

Some large Colombian municipalities, including Bogotá and Medellín, chose to use this new autonomy to strengthen their existing public utilities. A few, like Cartagena, decided to create mixed-capital companies to run their water and sanitation service, with the goal of retaining control of the service's assets and providing the necessary investment capital, while contracting an experienced private operator to improve management.

Cartagena brokered a deal with a Spanish company, Aguas de Barcelona, whereby the municipal government owns 50 percent of the resulting public-private entity, Aguas de Barcelona owns 46 percent and local private investors own the balance. Under the management contract, Aguas de Barcelona is paid 3.44 percent of revenues (around $1 million per year) to operate the service, and it has complete control over personnel and contracting decisions.

Though the system it inherited had many problems resulting from years of neglect—poor water quality, a heavily leaking pipe structure, other infrastructure in need of critical repairs—ACUACAR's greatest challenge lay in extending service to some 350,000 people who had no connections at all. With funds from the city and loans from the IDB and World Bank, the company has been able to extend in-home water connections to 98 percent of the city's population (up from 73 percent in 1995), and nearly 90 percent of Cartagena's residents now have access to sewer lines (up from 60 percent).

ACUACAR has succeeded in other areas as well. The biochemical quality of the water has long since been brought up to international standards. Water pressure, which used to be so low that most people had water for only a few hours each day, is now sufficient to provide 24-hour continuity in almost all of the city. And ACUACAR is completing treatment facilities capable of processing 80 percent of the city's wastewater.

Because of its success, ACUACAR enjoys a degree of credibility and public approval that is unusual for a water and sanitation service in Latin America. When Aguas de Barcelona announced plans to sell its stake in ACUACAR, Cartagena's municipal government found that customers didn't want the Spanish company to leave—quite a contrast to the suspicion and opposition that greeted the city's plan for a public-private partnership when it was first proposed in 1995.

BOX 11 • INFRAFUND

The Infrastructure Investment Fund (InfraFund) supports the preparation and development of sustainable infrastructure projects that are critical for the development of Latin America and the Caribbean. An IDB commitment of $20 million to the fund, launched in September of 2006, will facilitate Bank investments expected to surpass $12 billion over the next five years.

InfraFund is designed to assist public, private and mixed-capital companies in the region in identifying, developing and preparing bankable and sustainable infrastructure projects with real potential for achieving financial closure. Its resources can be used to hire specialized consulting services, conduct feasibility and other technical studies and carry out other activities aimed at preparing infrastructure projects for financing and completion. The fund also supports targeted measures to improve national and regional climates for investment in infrastructure.

While proposals for financing can be submitted for all sectors, the Bank encourages projects that mobilize private financing and promote public-private partnerships. The IDB targets sectors with significant, multiple developmental impacts, such as water and sanitation, and transportation, and those undertaken in the poorer countries. Operations with a high probability of reaching financial closure and those executed at the subnational level are also favored by the Bank.

InfraFund will actively participate in projects of the Initiative for the Integration of Regional Infrastructure in South America (IIRSA). The IDB is a permanent member of IIRSA´s Technical Coordination Committee and supports its projects with loans, grants and technical assistance.

Since its initiation, InfraFund has received expressions of interest in more than 50 infrastructure projects in different sectors from nearly 20 countries in the region.

These inquiries have come from the private and public sector windows of the Bank, the Inter-American Investment Corporation, the *Corporación Interamericana para el Financiamiento de Infraestructura* of Costa Rica and individual project sponsors. To date, the fund has reviewed 13 formal requests for support. Three of them were received through its website: **www.iadb.org/infrafund**.

The fund granted eligibility to seven projects and approved five of them for a total of $3.45 million by year-end 2006. One was an umbrella fund jointly financed with Brazil's National Development Bank and the International Finance Corporation that will be used to prepare infrastructure projects in Brazil. Resources for the other four technical cooperation operations will be used to prepare for specific projects expected to generate $1 billion in infrastructure investment with IDB participation.

InfraFund may receive financing from other donors, including governments and multilateral agencies, as well as private organizations. Funding from other sources is expected to become more important as InfraFund establishes a track record.

policy changes have included raising the cap on IDB loans and guarantees for private sector projects from $75 million to $200 million (and, in certain circumstances, $400 million), and allowing the Bank to finance up to 50 percent of the cost of expansion projects. The Bank also adopted policies that allow it to disburse loans and denominate partial credit guarantees in local currency, and to provide debt refinancing to firms in the region.

GUATEMALA • Through a microcredit program, rope manufacturer Fabián Lucas in San Antonio Ilotenango received bridge financing to help his business grow.

Private Sector Operations

During 2006, the Bank approved 20 private sector transactions totaling $920 million for projects with a total cost of $4.7 billion (compared to 16 transactions for $673 million in 2005). Of these, 12 projects included an IDB guarantee, while eight included IDB "A-loans." Ten of the guarantee transactions were under the auspices of the Trade Finance Facilitation Program. Several transactions supported local mortgage markets in the region, including operations in Chile, Mexico and Peru.

The Bank made permanent its regional Trade Finance Facilitation Program and its ability to issue IDB guarantees covering up to 100 percent of eligible trade-financing instruments. Under the program, which was launched in 2005, the IDB issues guarantees to international banks to mitigate the risk from eligible Latin American and Caribbean banks in export and import contracts with tenors of up to three years. The program now has a network of 20 issuing banks in 12 countries in the region and 77 confirming banks belonging to 36 international banking groups from 25 countries around the world. Through these financial institutions the IDB has issued guarantees for nearly $90 million in support of 110 individual trade transactions totaling $124 million.

In response to a decision made at the Annual Meeting of the Board of Governors in Belo Horizonte, Brazil, the Bank's management developed an integrated business plan for all of the Bank Group's private sector and non-sovereign-guaranteed operations. The plan calls for a substantial increase in the volume of activities and in the relevance of the IDB Group's private sector efforts in the region, as well as for a stronger presence in smaller countries and less-developed areas. It lays the groundwork for improved responsiveness to clients and operations based on country focus, establishes specific performance targets to ensure accountability and creates operational and administrative synergies for the implementation process. The plan also provides for an integrated approach between the Bank's public and private operations and with the Bank's local offices.

Multilateral Investment Fund

The MIF is an independent fund administered by the IDB. Its focus is to test and introduce new ways to strengthen micro- and small enterprise capacities, stimulate improve-

MEXICO • Women business owners in remote, low-income areas of Oaxaca received support from a microenterprise program.

ments in the business environment and engage the private sector in the development process. During 2006, the MIF approved 109 projects totaling $125 million. Of these, 97 were grants for $71 million and 12 were equity investments or loans for $54 million. Since its establishment, the MIF has approved $1.1 billion, net of cancellations, to finance 889 technical assistance and investment projects. Including counterpart funds, some $2.2 billion have been committed to MIF projects throughout the region.

Five of the MIF investments approved in 2006 were for innovative projects promoting new financial services, such as Afore Bansefi, a Mexican pension fund serving low-income and rural populations; Value Investments, a factoring fund for small businesses in Peru; and Paralife, a new life insurance company serving low-income and handicapped individuals. In addition, the MIF approved two new equity investment funds, one each for Argentina and Brazil, and a regional small business fund for Central America.

Continuing its leadership role in remittances, the MIF approved three new projects to enhance the development impact of remittance flows, improve central bank reporting and procedures and facilitate access to housing for remittance recipients. This brings the number of MIF remittances projects to 18. During the year, the MIF assisted the Asian Development Bank and the European Bank for Reconstruction and Development in adopting a remittance strategy for their regions of influence based on the MIF's experiences.

Other MIF activities during the year were promoting cleaner technologies for smaller enterprises; linking emigrant communities to local support for productive initiatives in Latin America and the Caribbean through hometown associations in the United States; and sustainable tourism.

In 2006, MIF member countries began depositing the necessary instruments of acceptance and contribution for the MIF replenishment approved in 2005 to become effective. France, Haiti, Sweden, Switzerland and the United Kingdom agreed to join the MIF, increasing membership to 38 countries and bringing important new expertise and ideas.

Inter-American Investment Corporation

The Inter-American Investment Corporation (IIC) is the only multilateral development finance institution in the world whose specific mission is to foster economic development by promoting the creation, expansion and modernization of small and medium-sized enterprises. The IIC, which began operations in 1989, provides financing to companies that do not have access to sufficient sources of credit or capital. Its operations create jobs, stimulate economic growth and help improve the standard of living in the region.

The IIC approves loans to and invests directly in small and medium-sized companies. Indirectly, it provides financing through financial intermediaries and equity funds. The IIC does not require sovereign guarantees. To be eligible for financing from the IIC, projects must foster sustainable development, create jobs, promote broader capital ownership, generate net foreign exchange, foster the transfer of resources and technology, use local resourc-

BOX 12 • NATURAL GAS MEGAPROJECT FUELS CHANGE IN PERU

For Peru, the $1.7 billion Camisea natural gas project was a major milestone in the country's bid for energy independence. By exploiting one of the largest natural gas reserves in Latin America, Camisea has already fulfilled its promise of giving the country long-term energy security. It is changing Peru's status from a net hydrocarbon importer to an exporter, and the country's industrial and residential customers are switching to this relatively non-polluting fuel.

The convenience of piped natural gas is being enjoyed in kitchens all over Lima.

Over the next three decades, the project is expected to add a percentage point annually to Peru's growth rate. A more robust economy will help improve living standards and increase tax revenue. Already gas royalties are financing new schools, health centers, roads, bridges and many other projects in hundreds of communities in the Camisea project area.

Beyond economic benefits, the Camisea project is applying a new strategy to reduce the negative impacts of hydrocarbon production in the Amazon.

For example, following stringent rules and guidelines, company crews worked in limited areas and took preventative actions to minimize contact with indigenous communities and prevent the transmission of disease. Construction activities were required to follow strict rules to minimize environmental degradation. Road construction was not done in key environmental areas. Workers in the natural gas production area were either transported on the Urubamba River or flown in by air.

For the private companies involved—Pluspetrol Perú and Transportadora de Gas del Perú—the regulations and working in the rainforest made an already complex project more challenging still. But 430 kilometers to the east, in Peru's capital of Lima, government officials were struggling with another set of issues. This was Peru's first energy megaproject, and they were charged with assembling the expertise needed to monitor—and impose sanctions where necessary—the laws and regulations governing Camisea's construction and operations.

This involved changes—new regulatory regimes, closer collaboration among agencies, new technical expertise, systems for anticipating and preventing conflicts—which add up to a foundation that will give the government the ability to exercise its responsibilities not only in Camisea, but in future megaprojects as well. And more such projects are on the horizon. The Peruvian Amazon is rich in hydrocarbon resources, and with soaring national and worldwide energy demand, new production investments are probable.

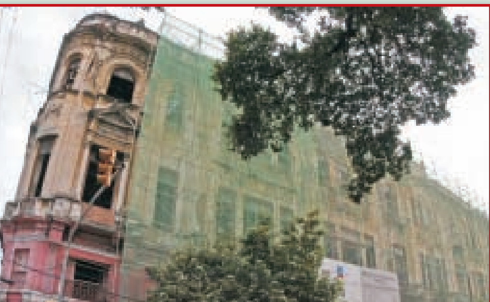
In addressing these daunting issues, the government has found a partner in the Inter-American Development Bank. In addition to a $75 million loan approved in 2003 to help finance a portion of the pipeline construction, the IDB also lent $5 million to strengthen the government's ability to monitor and ensure compliance with the project's environmental and social conditions.

Even before approving the two loans, and before construction had gotten underway, the IDB assigned a team of technical experts, both Bank staff and consultants, to work with the government institutions to improve project design, procedures and standards. Later, IDB specialists helped to supervise and monitor the environmental and social protection measures, both in advance of Bank financing in 2002 and subsequently.

Throughout its involvement, the IDB has held many meetings with stakeholders, both throughout Peru and in Washington, and will hold semiannual public meetings throughout the project's lifespan. The IDB is leveraging its minority financial contribution to Camisea to produce major benefits for the country and its citizens.

BOX 13 • SUBNATIONAL LENDING

New realities across the region mean that the Bank's clients have evolved to a universe that ranges from fully public to fully private sector. The Bank's new lending guidelines allow it to work seamlessly with the full spectrum of projects, regardless of ownership. The Bank can now lend directly to subnational public entities without sovereign guarantees. The adoption of this new approach for all potentially creditworthy projects enables the Bank to consider how best to mitigate project risk while scarce public funds can be used more efficiently in those areas where the central government's financial support is needed. This approach also allows project entities to achieve better corporate governance, transparency and institutional development.



Urban renewal is an area where partnerships between local and regional governments and the private sector can be promoted.

As local governments improve their own fiscal management capacity, they will have more opportunities to stimulate local economic development by undertaking infrastructure projects and other investments in partnership with the private sector without depending on the financial support of the government. A growing number of projects tap private participation in different ways to allocate investment, operational risk and management responsibilities, without necessarily transferring a majority ownership stake to the private sector.

The Bank's new approach to non-sovereign-guaranteed financing will serve subnational entities directly and enhance their ability to attract significant levels of private sector participation into public-private partnership arrangements. Lending criteria for such projects include creditworthiness, development impact, sound corporate governance, fiscal discipline and management effectiveness.

es in an ecologically sustainable manner, encourage local savings or promote regional integration.

In 2006, the IIC approved a record 46 operations for $338 million in 13 countries, including two regional operations. These operations will mobilize an additional $173 million from other sources to benefit small and medium-sized enterprises in the region.

The operations approved during the year were for companies in manufacturing, agribusiness and fisheries, infrastructure, health care and housing. In addition, the IIC continued its efforts to offer financing in local currency following its successful operation in Colombia. In 2006, it approved its first local-currency transaction in Peru, where the Corporation will provide local-currency loans to an estimated 1,400 micro-, small and medium-sized enterprises.

To meet the minimum eligibility requirements for IIC financing, a company must, among other prerequisites, provide a sound business plan, independently audited financial statements and proof that it meets IIC environmental protection and workplace safety standards.

Because many potential clients do not initially meet these requirements, in 2006 the IIC also channeled over $1 million in technical assistance to the region to assist companies requesting financing from the Corporation. Potential clients benefit from an independent assessment of their projects and advice on improving their design and financial structure. Implementation of good practices in these areas helps companies compete in the global economy.

For further information on the IIC's operations, see its 2006 Annual Report, which is published separately. For general information on the IIC and for data on prior-year operations, visit its website at **www.iic.int**.

Social Entrepreneurship Program

Under its Social Entrepreneurship Program, the Bank provides loans and grants to private, nonprofit and local or regional government organizations that offer financial, business, social and community development services to disadvantaged groups. This flexible instrument has helped the Bank expand its activity to sectors where international financing has been scant,


ARGENTINA • Professor Silvia Moreno of the University of Buenos Aires conducts research under a technology modernization program.

explore new fields of endeavor and devise cutting-edge solutions to the region's most disadvantaged communities.

In 2006 the Bank approved 16 such projects for a total of $11.1 million, 64 percent loans and 36 percent grants. Among the most innovative initiatives were a program in Peru to promote the labor market and the entrepreneurial development of physically challenged adults, and a system to generate sustainable income for groups of microenterprises in poor communities in Colombia through corporate social responsibility programs managed by large companies.

The IDB continues to play a leadership role in supporting microenterprise in the region. The Ninth Inter-American Forum on Microenterprise, organized by the Bank in September in Ecuador, attracted more than 1,300 private and public sector participants from 37 countries. The forum serves as an increasingly important platform for the exchange of best practices and the discussion and promotion of strategies to overcome challenges to microenterprise development in Latin America and the Caribbean.

RISK MITIGATION AND INTEGRITY

Various Bank units share responsibility for administering risk mitigation. The Office of the Auditor General focuses on corporate risk management, with an emphasis on financial reporting. The Finance Department is responsible for general risk management. The Development Effectiveness and Strategic Planning Department administers the Bank's portfolio management system, which detects "problem" projects and flags them early through a system of alerts, and it prepares the Annual Report on Portfolio Management, Execution and Results. The Office of Private Sector Credit Risk Assessment provides an independent judgment of the credit and portfolio risk of all private sector operations. During 2006 it worked to develop a new credit risk classification system for all private and non-sovereign-guaranteed operations that will be rolled out during 2007. The Bank's Office of Institutional Integrity (OII) coordinates many activities related to combating corruption as both a corporate and development priority and takes the lead in detecting, investigating and preventing fraud, corruption and misconduct in Bank operations.

In 2006, the OII, an independent office reporting directly to the IDB president, received 183 new inquiries: 149 were allegations of fraud, corruption or misconduct and the rest were consultations related to the Bank's anti-corruption policies. Approximately 90 percent of the allegations concerned fraud or corruption in Bank-financed activities and the remaining 10 percent related to staff misconduct, involving alleged violations of the Code of Ethics or other staff rules. During this period, the OII completed 123 investigations, more than 80 percent of which concerned fraud and corruption in Bank-financed activities. Where the OII found that the allegations were substantiated, it recommended courses of action to the Oversight Committee on Fraud and Corruption, such as

BRAZIL • Workers build an overpass for a mass transit project in Porto Alegre.

referrals of findings to national authorities or other remedial measures. The OII annual report is available at **www.iadb.org/integrity**.

The Office of Oversight and Evaluation reports to the Board of Executive Directors. It plays a dual role, evaluating overall Bank activities and conducting studies on country-level, thematic, sectoral and policy- and instrument-related issues. Its reports are available at **www.iadb.org/ove/**.

In September 2006, the Bank approved new sanctions procedures, including a new Sanctions Committee. The sanctions procedures are designed to strengthen the existing rights of all parties involved, while ensuring that the Bank is able to perform its investigative function effectively. The Sanctions Committee holds responsibility for determining when sanctions should be imposed on firms or individuals found to have violated the Bank's anticorruption policies. Decisions by the Sanctions Committee are based on the investigative findings of the OII and submissions of the parties and are made public. The Bank also approved updated ethics and conduct guidelines for staff in 2006.

The Year's Lending

BOLIVIA • Schoolchildren in a low-income neighborhood outside La Paz attend a school built and furnished under a community development program.

GUATEMALA • A health worker checks a baby's weight at a clinic in La Unión near Quetzaltenango as part of an innovative plan to bring health care to poor rural areas.

THE YEAR'S LENDING

SUMMARY

The 2006 loans and guarantees approved by the Bank and cumulative totals, as of December 31, 2006, less cancellations, came from the following sources:

▶ **Ordinary Capital (OC):** 90 loans for $5.4 billion and 13 guarantees for $393 million brought the cumulative total of loans to 1,868 for $124 billion and the cumulative number of guarantees to 30 totaling $994 million.

▶ **Fund for Special Operations (FSO):** 23 loans totaling $602 million brought the cumulative total of loans to 1,197 for $18.3 billion. In addition, one guarantee for $3 million was approved.

FIGURE 6. LENDING BY SECTOR, 2006

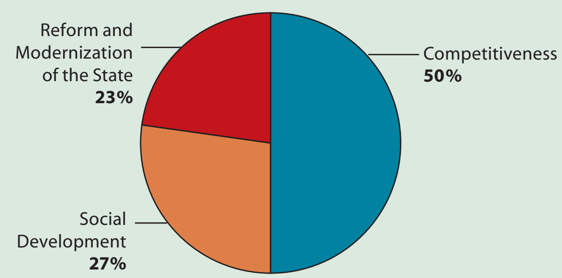
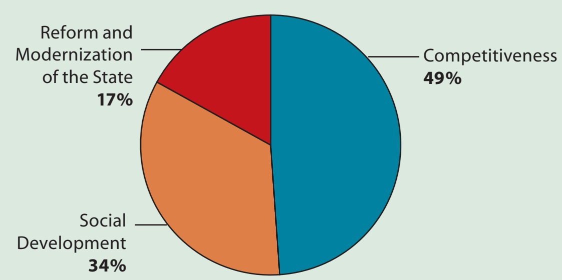


FIGURE 7. LENDING BY SECTOR, 1961-2006



GUATEMALA • **The Samalá III bridge was one of 66 rebuilt after Hurricanes Mitch and Stan as part of emergency financing for disaster relief and reconstruction.**

TABLE II • DISTRIBUTION OF LOANS AND GUARANTEES BY SECTOR OF ACTIVITY[1]
(In millions of U.S. dollars)

SECTOR	2006	%	1961–2006	%
Competitiveness	**$ 3,190.1**	**50.0**	**$ 71,846.3**	**49.5**
Energy	1,044.4	16.4	20,077.3	13.8
Transportation and Communication	717.3	11.2	15,777.0	10.9
Agriculture and Fisheries	62.1	1.0	13,612.2	9.4
Industry, Mining and Tourism	5.0	0.1	12,750.3	8.8
Multisector Credit and Preinvestment	0.0	0.0	3,638.6	2.5
Science and Technology	331.5	5.2	1,936.1	1.3
Trade Financing	252.9	4.0	2,345.1	1.6
Productive Infrastructure	333.3	5.2	1,175.9	0.8
Capital Markets	443.6	7.0	533.9	0.4
Social Development	**1,727.1**	**27.1**	**48,593.9**	**33.5**
Social Investment	994.5	15.6	19,867.6	13.7
Water and Sanitation	370.0	5.8	9,473.4	6.5
Urban Development	74.4	1.2	7,446.1	5.1
Education	60.5	0.9	5,579.9	3.8
Health	140.0	2.2	2,981.5	2.1
Environment	84.8	1.3	2,753.0	1.9
Microenterprise	2.9	0.0	492.3	0.3
Reform and Modernization of the State	**1,463.7**	**22.9**	**24,579.8**	**16.9**
Reform and Public Sector Support	24.3	0.4	11,383.5	7.8
Financial Sector Reform	801.0	12.6	7,406.3	5.1
Fiscal Reform	177.0	2.8	4,040.7	2.8
Decentralization Policies	353.0	5.5	1,072.5	0.7
Modernization and Administration of Justice	54.0	0.8	368.9	0.3
Planning and State Reform	26.4	0.4	143.3	0.1
Parliamentary Modernization	0.0	0.0	71.9	0.0
Civil Society	0.0	0.0	22.0	0.0
Trade Policy Support	0.0	0.0	27.4	0.0
E-Government	28.0	0.4	43.3	0.0
TOTAL	**$6,380.9**		**$145,020.0**	

[1] Categories reflect priority areas of activity according to the Bank's Institutional Strategy.

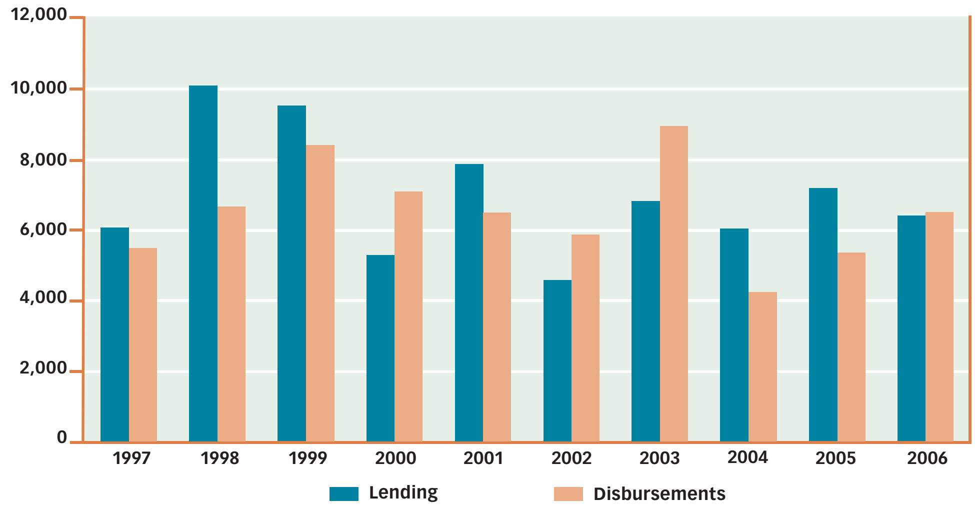
TABLE III • YEARLY (2006) AND CUMULATIVE (1961–2006) LENDING INFORMATION[1]

(In millions of U.S. dollars)

	TOTAL COST OF PROJECTS		LOANS AND GUARANTEES APPROVED[1]					DISBURSEMENTS				
	Total Amount		Total Amount[3]		Ordinary Capital[2,3]	Fund for Special Operations	Funds in Administration	Total Amount		Ordinary Capital[2]	Fund for Special Operations	Funds in Administration
Country	2006	1961–2006	2006	1961–2006	1961–2006	1961–2006	1961–2006	2006	1961–2006	1961–2006	1961–2006	1961–2006
Argentina	$ 2,178.2	$ 47,261.1	$ 1,625.7	$ 22,657.4	$ 21,963.4	$ 644.9	$ 49.1	$ 1,109.5	$ 18,868.3	$ 18,174.3	$ 644.9	$ 49.1
Bahamas	0.8	785.9	8.8	380.4	378.4	—	2.0	7.1	308.5	306.5	—	2.0
Barbados	11.5	597.4	0.7	420.3	361.1	40.2	19.0	2.2	323.3	264.1	40.2	19.0
Belize	25.0	170.2	25.0	112.3	112.3	—	—	12.4	87.8	87.8	–	—
Bolivia	162.7	6,172.7	153.0	3,735.8	1,235.4	2,427.1	73.3	62.7	3,220.4	1,214.7	1,932.4	73.3
Brazil	1,824.0	86,085.9	515.7	28,675.4	26,986.2	1,556.0	133.2	1,733.1	25,773.6	24,087.9	1,552.4	133.3
Chile	667.2	13,129.0	213.3	5,426.8	5,178.7	204.2	43.9	31.0	4,978.6	4,730.5	204.2	43.9
Colombia	775.0	24,923.5	620.0	12,809.8	11,982.7	762.8	64.3	950.5	11,896.3	11,072.8	759.2	64.3
Costa Rica	83.4	4,136.2	70.0	2,488.5	1,992.9	357.5	138.1	24.0	2,149.9	1,661.8	357.5	130.6
Dominican Republic	183.5	4,125.2	181.0	3,028.0	2,204.3	736.1	87.6	118.1	2,423.6	1,599.9	736.1	87.6
Ecuador	514.0	8,930.6	326.9	4,573.7	3,527.3	956.3	90.1	160.9	4,089.6	3,043.2	956.3	90.1
El Salvador	102.5	5,075.7	102.5	3,287.3	2,361.3	778.2	147.8	91.7	2,761.5	1,845.5	778.2	137.8
Guatemala	239.5	4,666.3	239.0	2,918.2	2,197.9	650.1	70.2	130.3	2,372.6	1,661.3	650.1	61.2
Guyana	122.2	1,272.3	116.7	1,085.2	115.9	962.4	6.9	46.5	791.2	115.9	668.4	6.9
Haiti	101.2	1,768.5	100.4	1,280.9	—	1,274.5	6.4	65.7	791.0	—	784.7	6.3
Honduras	129.4	4,892.5	125.9	2,877.8	564.4	2,247.9	65.5	92.0	2,335.4	542.7	1,740.6	52.1
Jamaica	5.0	2,380.3	5.0	1,774.8	1,407.4	168.5	198.9	25.9	1,643.6	1,276.2	168.5	198.9
Mexico	1,510.0	51,200.1	387.0	19,486.9	18,870.0	559.0	57.9	677.0	17,410.6	16,793.7	559.0	57.9
Nicaragua	146.0	4,002.0	132.5	2,478.2	280.6	2,131.6	66.0	123.8	2,034.6	272.6	1,709.7	52.3
Panama	318.1	3,008.7	304.7	2,434.5	2,101.6	290.2	42.7	139.8	1,928.4	1,604.4	290.2	33.8
Paraguay	780.3	14,161.3	257.2	2,160.3	1,544.8	602.5	13.0	72.5	1,703.2	1,087.7	602.5	13.0
Peru	358.2	5,538.1	565.0	7,737.8	7,084.6	432.0	221.2	467.5	6,909.3	6,256.1	432.0	221.2
Suriname	—	126.1	—	104.7	102.7	2.0	—	7.7	69.8	67.8	2.0	—
Trinidad and Tobago	35.0	1,642.2	28.0	1,070.5	1,014.7	30.6	25.2	23.8	878.5	822.7	30.6	25.2
Uruguay	217.5	5,578.0	190.9	4,197.9	4,051.9	104.2	41.8	114.8	3,570.2	3,424.1	104.2	41.9
Venezuela	51.0	16,430.9	26.0	4,848.4	4,674.1	101.4	72.9	73.0	3,789.7	3,615.4	101.4	72.9
Regional	150.0	17,730.2	60.0	2,968.2	2,717.8	236.7	13.7	125.9	2,542.3	2,308.1	220.5	13.7
TOTAL	**$10,691.2**	**$335,790.9**	**$6,380.9**	**$145,020.0**	**$125,012.4**	**$18,256.9**	**$1,750.7**	**$6,489.4**	**$125,651.8**	**$107,937.7**	**$16,025.8**	**$1,688.3**

[1] After cancellations and exchange adjustments. Totals may not add up due to rounding.
[2] Detail includes non-sovereign-guaranteed loans, net of participations.
[3] Includes authorized lines of credit from inception to date in the aggregate amount of $423 million ($153 million for 2006) under the Trade Finance Facilitation Program.

FIGURE 8. LENDING AND DISBURSEMENTS, 1997–2006
(In millions of U.S. dollars)



▶ **Other funds:** There was one loan for $2.5 million approved in 2006. Cumulative total loans were 210 for $1.8 billion.

The Bank agreed to partially defray up to five percentage points of the interest on 10 loans for $365 million, approved in 2006 from the Ordinary Capital, with funds from the Intermediate Financing Facility (IFF) created under the Sixth Replenishment.

Total Cost of Projects

The $6.4 billion in Bank loans and guarantees approved in 2006 will help to finance projects involving a total investment of $10.7 billion. The Bank's loans cover only a part of the total cost of the projects being carried out by the borrowing countries. The balance comes principally from the Latin American and Caribbean countries.

Disbursements

The Bank's disbursements on approved loans amounted to $6.5 billion in 2006, compared with $5.3 billion in 2005. As of December 31, 2006, cumulative disbursements, including exchange adjustments, totaled $125.7 billion, or 87 percent of the loan amounts approved by the Bank. The 2006 disbursements and cumulative totals as of December 31, 2006 by funds include the following:

▶ **Ordinary Capital:** $6.1 billion, bringing the cumulative total to $107.9 billion.

▶ **Fund for Special Operations:** $398 million, bringing the cumulative total to $16 billion.

▶ **Other funds:** $3 million, bringing the cumulative total from funds administered by the Bank to $1.7 billion.

For information on disbursements for the purchase of goods and services by country of origin, see Tables XIII and XIV in the CD-Rom.

Repayments

Loan repayments amounted to $8.9 billion in 2006. Cumulative repayments as of December 31, 2006, were $70.1 billion. Repayments received by the Bank during the year, and cumulative as of December 31, 2006, were as follows:

▶ **Ordinary Capital:** $8.6 billion, bringing the cumulative total, excluding repayments to participants, to $60.9 billion.

▶ **Fund for Special Operations:** $290 million, for a cumulative total of $7.6 billion.

▶ **Other funds:** $3.2 million, bringing the cumulative total to $1.6 billion.

For more information on IDB operations, see Table XI, "Ten Years of IDB Operations, 1997-2006," in the CD-Rom. Information on IDB projects is available at **www.iadb.org/projects/**.

TABLE IV • STATEMENT OF APPROVED OPERATIONS[1] (ABOVE $1 MILLION), 2006

(In millions of U.S. dollars)

COUNTRY	PROJECT	FUND	AMOUNT
Argentina	Norte Grande Electricity Transmission Program	OC	580.0
	Public Finance Management Sector	OC	500.0
	Technological Modernization Program III	OC	280.0
	Social Development of Córdoba Province	OC	180.0
	Program for Development of Satellite System and Applications	OC	50.0
	Lending Program for Productive and Job Development in the Province of San Juan	OC	32.6
	Investment Fund for Small and Medium-Sized Enterprises TGLT Ventures I	MIF	5.1
	Strengthening Competitiveness of Clusters in the Central Region of Santa Fe Province	MIF	1.9
	Human Resources Management in a New Labor Relations Framework	MIF	1.4
	Consolidation of Wine Tourism	MIF	1.0
Bahamas	Natural Risks Preventive Management	OC	5.0
	Masterplan for Coastal Zone Management	OC	3.8
Barbados	Total operations[2]	MIF	0.9
Belize	Macroeconomic and Public Financial Sector Reform Program	OC	25.0
Bolivia	Santa Bárbara–Rurrenabaque Northern Corridor Highway Improvement	FSO	120.0
	Program to Consolidate Reforms in the Government Revenues Area	FSO	15.0
	Corporate Enhancement Support Fund	FSO	10.0
	Banco de Crédito de Bolivia	OC	8.0
	Jesuit Missions in the Chiquitania	MIF	1.4
	Competitiveness of Agrifood Chains in the Central Valley of Tarija	MIF	1.1
Brazil	Coelba Investment Program[3]	OC	112.0
	ATE II Energy Transmission Line[4]	OC	107.8
	States and Federal District Administration Modernization I—PNAGE	OC	93.0
	Celtins Investment and Refinancing Program[5]	OC	60.0
	Coke Production and Integrated Cogeneration[6]	OC	50.0
	São Paulo State Highways Phase II	OC	30.0
	Banco Industrial e Comercial S.A.[7]	OC	20.0
	Fiscal Management in the State of Bahia	OC	12.0
	Banco Pine	OC	11.0
	Program to Strengthen Business Activity in the State of Bahia	OC	10.0
	Banco Industrial do Brasil	OC	6.0
	FIPAC Investment Growth Fund for Brazilian Technology-Based SMEs	MIF	5.1
	Stratus VC III Investment Fund for Technology-Based SMEs	MIF	4.4
	Strengthening of Institutional Capacity for Regulatory Management	OC	3.9

Key: OC, Ordinary Capital; FSO, Fund for Special Operations; MIF, Multilateral Investment Fund.

1 Includes authorized lines of credit under the Trade Finance Facilitation Program.

2 There were no projects approved above $1 million. The amount reflected is the total approvals for the year.

3 Complemented by a "B" loan syndication of approximately $70 million.

4 Complemented by a "B" loan syndication of approximately $11.8 million.

5 Complemented by a "B" loan syndication of approximately $20 million.

6 Complemented by a "B" loan syndication of approximately $350 million.

7 Increase to line of credit authorized in 2005.

(Continues on next page)

TABLE IV • STATEMENT OF APPROVED OPERATIONS[1] (ABOVE $1 MILLION), 2006
(Continued)

COUNTRY	PROJECT	FUND	AMOUNT
Brazil (cont.)	Investment Fund for Emerging Technology-Based Companies (Rio Bravo Investech II)[8]	MIF	2.4
	Sustainable Development of Wood and Furniture Supply Chain in the Amazon Region	MIF	2.1
	Corporate Social Responsibility through Support for Local Productive Initiatives	MIF	1.1
	Support for Environmentally Sustainable Integrated Production	MIF	1.1
	Brazilian PPP Development Fund	OC	1.0
Chile	Securitizadora Security GMAC-RFC	OC	80.0
	Subnational Management Support Program (CCLIP)	OC	50.0
	Integrated Development for Indigenous Peoples, Phase II	OC	45.2
	Regional Productive Development Agencies	OC	20.0
	Charrua-Temuco Transmission Line[9]	OC	17.0
	Strengthening the Job Training Industry	MIF	2.0
	External Certification of ISO Norms/Public Management	OC	1.6
Colombia	Competitiveness in Colombia I	OC	200.0
	Social Reform and Equity I	OC	200.0
	Education Equity in Bogotá	OC	60.0
	Roads for Integration and Social Equality	OC	60.0
	Expansion of Health Services Networks Program Phase I	OC	50.0
	Banco de Bogotá	OC	40.0
	Citizen Services Quality Improvement Program	OC	10.0
	The Role of Remittances in the Development of the Low-Income Housing Market	MIF	1.7
	Preparation of Río Bogotá Environmental Management Program	OC	1.5
	Preparation of the Infrastructure Project for the Pasto–Mocoa Road	OC	1.3
Costa Rica	Urban Poverty Alleviation	OC	50.0
	Tourism Program in Protected Areas	OC	20.0
	Complementary Studies for Hydroelectric Project El Diquís (Boruca-Veraguas)	OC	1.5
	Rural Community Tourism in Costa Rica and Replication in Central America	MIF	1.1
Dominican Republic	Social Management Reform Program	OC	150.0
	Program to Modernize Public Resource Management	OC	21.0
	Property Jurisdiction Consolidation	OC	10.0
	Opportunities and Technical Requirements for Gaining Market Access under DR-CAFTA	MIF	1.2
Ecuador	Universal Health Insurance Program (PAUS) Phase I	OC	90.0
	Environmental Sanitation Program Quito Metropolitan Phase I	OC	70.0
	Potable Water and Sanitation for Cuenca	OC	61.3
	Competitiveness Improvement I	OC	50.0
	Municipal Modernization and Neighborhood Improvement Phase I	OC	37.1
	Banco de Guayaquil	OC	12.0
	Renewal of Downtown Areas and Land Management in Cuenca	OC	6.6

[8] Increase to equity investment approved in 2002.
[9] Complemented by a "B" loan syndication of approximately $34 million.

(Continues on next page)

TABLE IV • STATEMENT OF APPROVED OPERATIONS[1] (ABOVE $1 MILLION), 2006
(Continued)

COUNTRY	PROJECT	FUND	AMOUNT
El Salvador	Social Policy Support Program	OC	100.0
	Promoting Financial Democracy by Supporting FEDECREDITO	MIF	3.3
	Creating a Housing Finance Market for Transnational Families	MIF	2.8
Guatemala	Public Financial Management	OC	100.0
	Social Investment Program for the Reduction of Rural Poverty	OC	50.0
	Rural Economic Development	OC	30.0
	Petén Development Program for the Conservation of the Maya	OC	30.0
	Violence Prevention Support Program	OC	29.0
Guyana	Support for Competitiveness Program	FSO	26.7
	Modernization of the Justice Administration System	FSO	25.0
	Transport Infrastructure Rehabilitation Program	FSO	24.3
	Georgetown Solid Waste Management	FSO	20.6
	Citizen Security Program	FSO	19.8
Haiti	Financial Sector Reform Support Program	FSO	25.0
	Rehabilitation of the Electricity Distribution System in Port-au-Prince	FSO	18.1
	Rural Supply Chain Development Program	FSO	17.8
	Rural Water and Sanitation Program	FSO	15.0
	Supplement II to the Transport Infrastructure Rehabilitation Program	FSO	14.5
	Support for Human Resource Management in the Public Sector	FSO	10.0
Honduras	Public Management Reform Program	FSO	30.0
	Social Interest Housing Program	FSO	30.0
	Supplemental Water Supply and Sanitation Investment Program	FSO	30.0
	Social Sector Program to Support the Poverty Reduction Strategy	FSO	27.9
	Banco FICOHSA	OC	8.0
	Local Ethnotourism Business Networks	MIF	1.4
Jamaica	First Global Bank Limited	OC	5.0
Mexico	Strengthening States and Municipalities II	OC	200.0
	Metrofinanciera Mortgage Warehouse and MBS Guarantee Facilities	OC	105.0
	Su Casita MBS Guarantee Facility	OC	75.0
	"Three for One" Pilot Project for Migrants	OC	7.0
	Capital Investment in Afore de la Gente (BANSEFI)	MIF	3.0
	Economic Reactivation after a Natural Disaster: Support for Small Businesses	MIF	2.5
	Tourism Development for MSMEs in the Tequila Region	MIF	1.6
Nicaragua	Acoyapa - Costa Rican Border Road Integration Program	FSO	49.5
	Social Sector Program in Support of the ERCERP	FSO	30.0
	Potable Water and Sanitation Investment Program	FSO	30.0
	Comprehensive Child Care Program	FSO	15.0
	Banco de Crédito Centroamericano S.A. (BANCENTRO)	OC	8.0
	Results-Based Public Management System Implementation	OC	1.6
Panama	Investment Climate and Trade Adjustment	OC	100.0
	Multiphase PPP Road Infrastructure for Competitiveness Program	OC	70.0
	Panama City and Bay of Panama Sanitation Project I	OC	45.0

(Continues on next page)

TABLE IV • STATEMENT OF APPROVED OPERATIONS[1] (ABOVE $1 MILLION), 2006
(Continued)

COUNTRY	PROJECT	FUND	AMOUNT
Panama (cont.)	Rural Electrification Program	OC	30.0
	Sustainable Development for Chiriqui Region Phase I	OC	27.0
	Comprehensive Security Program	OC	22.7
	Management Strengthening of the Maritime Authority of Panama	OC	5.0
	Investment Climate and Trade Adjustment Program	OC	5.0
Paraguay	Paving of Integration Corridors and Road Rehabilitation and Maintenance Phase I	OC	134.0
	ANDE's Multiphase Power Transmission Program Phase I	OC	69.5
	Modernization of Agricultural Support Management	OC	31.5
	Strengthening the Judiciary System	OC	6.3
	Interbanco	OC	5.0
	Professionalism of the Civil Service	OC	4.2
	INCOOP Institutional Strengthening Program	OC	3.6
	Promotion of Tourism to the Missions in the Guaraní World	MIF	1.8
Peru	Public Expenditure Management Quality Improvement II	OC	200.0
	National Highway System Serviceability Improvement Program	OC	100.0
	Banco Continental Financing Facility[10]	OC	120.0
	Guarantee for IIRSA Northern Amazon Hub	OC	60.0
	Decentralized Rural Transport (DRTP)	OC	50.0
	Banco Internacional del Perú-Interbank	OC	30.0
	Border Crossings	OC	5.0
	Cluster Promotion Program	MIF	2.7
	Small Business and Microenterprise Development Agency *Crear Arequipa*	MIF	2.6
	Promoting of Entrepreneurship at the Base of the Pyramid	MIF	1.3
	Leveraging the Capital Markets to Increase Financing for Small Enterprises through Factoring	MIF	1.1
	Assistance to SMEs on Technical Requirements for Gaining Market Access under the FTA	MIF	1.0
Suriname	Total operations[2]	OC, FSO	0.8
Trinidad and Tobago	E-Government and Knowledge Brokering Program	OC	28.0
Uruguay	Montevideo Sanitation Program (PSU IV)	OC	118.6
	Tax Administration and Public Expenditures	OC	50.0
	Clusters Competitiveness and Value Chains	OC	9.0
	Competitiveness of Tourist Destinations	OC	5.0
	Tax Management Support	OC	4.5
	Comprehensive Support for Dynamic Entrepreneurship	MIF	3.2
	Support for Civil Service Reform	OC	1.4
	Program to Improve Expense and Budget Process Quality	OC	1.4
Venezuela	INE and SEN Strengthening and Modernization Program	OC	25.0

[10] Complemented by a "B" loan syndication of approximately $80 million.

(Continues on next page)

TABLE IV • STATEMENT OF APPROVED OPERATIONS[1] (ABOVE $1 MILLION), 2006
(Continued)

COUNTRY	PROJECT	FUND	AMOUNT
Regional	Central American Mezzanine Infrastructure Fund	OC	60.0
	Local Currency Fund for Microfinance Institutions	MIF	10.3
	Investment Fund for Competitive SMEs (CASEIF) II	MIF	7.6
	Enhancing Financing to Small and Microenterprises through Innovative Techniques	MIF	5.3
	Voluntary Return Migration Model Based on Entrepreneurship Development	MIF	4.0
	Promoting Diaspora and Local Support for Productive Initiatives	MIF	3.3
	Assistance for SMEs in Central America on Technical Requirements for Access to DR-CAFTA	MIF	3.1
	Paralife: Insurance for Disabled People, Low Income People and Microentrepreneurs	MIF	3.0
	PRODEV Complementary Expenses	OC	1.8
	Application of General Principles for Remittances Markets	MIF	1.8
	Regional System for Assessment and Development of Citizen Competencies	OC	1.5
	Harmonized Regional Quality Infrastructure for Improving Market Access	MIF	1.4
	Food Fortification with Folic Acid and Other Micronutrients	OC	1.4
	Hydrocarbons Market Integration in Mesoamerica	OC	1.3
	Latin American Research Networks	FSO	1.3
	Colombia–Panama Electric Interconnection	OC	1.2
	Conservation of the National Resource Endowment of the Great Chaco	OC	1.2
	Strategy for the Introduction of Natural Gas in Central America	OC	1.2

For more information on IDB projects, see the online project database at **www.iadb.org/projects.**

TECHNICAL COOPERATION

A total of 442 technical cooperation projects for $104 million were approved in 2006. The IDB funds its grant program for technical cooperation with resources from the net income of the FSO, donor trust funds and the Ordinary Capital. In 2006, the FSO funded $24 million, donor trust funds $46 million and the Ordinary Capital $34 million.

For *social sector support*, 153 projects were approved for a total of $27 million. They aim to promote social equity, improve efficiency in social spending and strengthen support systems for social programs. The sectors in which these projects were carried out include education, rural development, microenterprise, youth, violence prevention and protection of vulnerable groups, urban development and environmental protection.

Projects for *competitiveness* included 158 operations approved for a total of $36 million. The Bank provided support to its borrowing member countries for their own initiatives to improve competitiveness through the deployment of productive infrastructure, the use of innovative technology and support for small and medium-sized enterprises. The Bank also provided supported various trade and sustainable development initiatives.

The program for *modernization of the state* included approvals in 92 projects for $25 million, comprising projects to strengthen the institutional, regulatory and management areas of government entities, as well as good governance and results-based management in taxation, fiscal management, customs and public spending. E-government and information technology were also important areas supported by the Bank.

In the *regional integration area*, 39 projects were approved totaling $16 million. The Bank continued to focus on supporting countries in their integration processes at the subregional, hemispheric and international levels, with special emphasis on trade. Technical assistance was also provided for consolidation of subregional integration schemes.

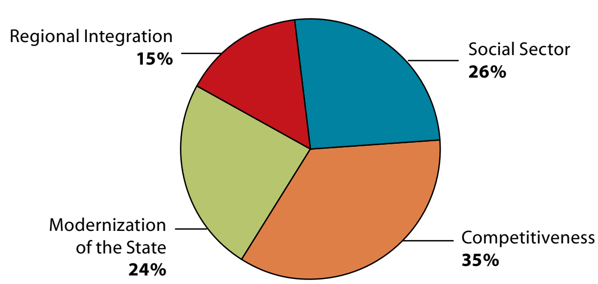
This year the Bank allocated $34 million to special programs/grants, accounting for almost one-third of the grants provided by the Bank. Two new programs for technical cooperation were approved by the Board of Executive Directors during the year: the Disaster Prevention Fund and the Infrastructure Project Preparation Fund (InfraFund). These new funds supplement other special programs estab-

TABLE V • DISTRIBUTION OF NONREIMBURSABLE TECHNICAL COOPERATION[1]
(In thousands of U.S. dollars)

Country	2006	1961–2006
Argentina	$ 2,400	$ 71,995
Bahamas	222	18,970
Barbados	33	21,220
Belize	693	7,852
Bolivia	1,403	84,468
Brazil	3,121	167,370
Chile	3,217	17,703
Colombia	10,046	70,813
Costa Rica	3,206	51,860
Dominican Republic	639	57,156
Ecuador	5,474	76,555
El Salvador	4,031	60,720
Guatemala	3,259	64,268
Guyana	3,751	58,903
Haiti	2,629	59,333
Honduras	3,125	74,665
Jamaica	779	40,247
Mexico	1,525	28,762
Nicaragua	4,843	81,955
Panama	1,698	40,130
Paraguay	2,642	68,835
Peru	4,379	93,182
Suriname	984	29,899
Trinidad and Tobago	509	21,042
Uruguay	3,654	36,312
Venezuela	18	12,317
Regional	35,280	828,785
TOTAL	**$103,562**	**$ 2,245,317**

[1] Does not include Social Entrepreneurship Program Financings.
Note: Totals may not add up due to rounding.

FIGURE 9. NONREIMBURSABLE TECHNICAL COOPERATION BY SECTOR, 2006
(percentage of total amount)



BAHAMAS • Digital mapping provides online data to government and nongovernmental organizations about the country's 700 islands.

lished previously: the Program for Development Effectiveness (PRODEV), the IDB Integration Fund, which supports regional infrastructure initiatives, and the Initiative for the Promotion of Regional Public Goods.

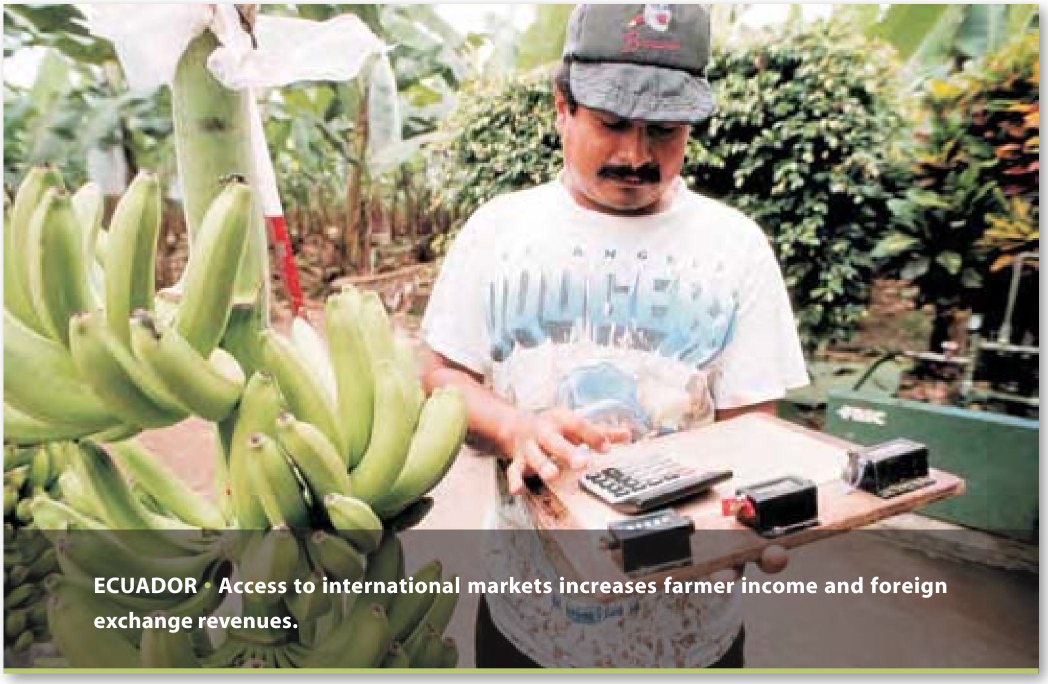
COFINANCING

In 2006 multilateral and bilateral cofinancing transactions, not counting private sector loans, the IIC, the MIF or trust fund operations, totaled a record amount of over $3.6 billion. The number of cofinanced projects and beneficiary countries also reached new highs. This steady progression in the IDB's cofinancing operations is attributable to several factors: deepening programmatic cooperation with multilateral and bilateral partners, successful strategic partnerships, renewed interest in regional infrastructure programs, a more attractive lending framework and Bank-wide mainstreaming of cofinancing as a common instrument to improve development effectiveness.

Cofinancing benefits all the parties involved: borrowing member countries gain access to larger and more diversified capital inflows with favorable financial conditions and to technical assistance; donors can realize more effective development contributions at lower transaction costs; and the IDB benefits from broader support for policy-based lending and sector-wide operations, with less restrictive investment and risk ceilings.

The record cofinancing involved 13 partners supporting 38 operations in 18 countries, including a regional operation in Central America. Several operations attracted multiple donors, including new partners. The World Bank once again was the IDB's principal cofinancing partner, cofunding 24 projects in 12 countries. Other important multilateral contributors were the Andean Development Corporation (CAF), Central American Bank for Economic Integration (CABEI), Organization of Petroleum Exporting Countries (OPEC) Fund, European Union and Global Environment Fund. Sizeable bilateral support was received from Kreditanstalt für Wiederaufbau (KfW) of Germany, Japan Bank for International Cooperation (JBIC) and Swedish International Development Cooperation Agenda (SIDA). Roughly two-fifths of the cofinancing volume was for social investment projects and just over one-third for infrastructure and competitiveness projects, with the remainder supporting various sector reform programs.

In addition, a quantum leap was made in attracting special untied grants known as COFABs, which have fast-track approval and flexible implementation procedures to ensure timeliness. After averaging just $2 million annually from 2002 to 2005, COFAB grants soared to $44 million in 2006. The donations were obtained from Canada, the European Union, Finland, Germany, Spain, Switzerland and the United Kingdom. The grants supported such activities as renewable energy, energy efficiency and carbon finance, indigenous entrepreneurial development, social cohesion and various targeted interventions and policy improvements. The largest contributions were for vocational train-



ECUADOR • Access to international markets increases farmer income and foreign exchange revenues.

ing in Haiti, municipal investment programs in Brazil and water and sanitation projects in Nicaragua and Haiti. As is customary, several private sector contributions sponsored activities to support microenterprise development and corporate social responsibility.

Nonfinancial activities in 2006 included staff seminars on public-private partnerships, infrastructure and related issues in conjunction with the European Investment Bank and Spain's Institute for Official Credit, both recent signatories of Memorandums of Understanding with the Bank. In May 2006 another Memorandum of Understanding was signed between the Bank and the OPEC Fund for International Development, aimed at deepening the future cooperation between the two institutions.

FUNDS IN ADMINISTRATION

Trust funds have become the largest source of financing for the Bank's nonreimbursable technical cooperation projects. The funds are established by donors to provide support to IDB borrowing member countries through consulting services, training and cofinancing for Bank loans and the Social Entrepreneurship Program. In 2006, trust fund donors contributed $36 million and the Bank administered 44 active trust funds for technical cooperation activities (see Table XII in the CD-ROM). Of the total $104 million in technical-cooperation grants approved during the year, $46 million came from trust fund resources. Of this total, Japanese trust funds accounted for $17.6 million, followed by Spanish funds with $6.6 million and multidonor funds with $6.4 million.

TABLE VI • COFINANCING IN 2006[1]
(In millions of U.S. dollars)

Cofinancier	Amount
Multilateral Institutions	
Andean Development Corporation (CAF)	$ 659.50
Central American Bank for Economic Integration (CABEI)	14.63
European Commission (EC)	4.27
Global Environment Facility (GEF)	8.50
International Atomic Energy Agency (IAEA)	0.10
Organization of the Petroleum Exporting Countries (OPEC)	13.60
World Bank Group (IBRD/IDA)	2,806.70
Subtotal	**3,507.30**
Bilateral Contributions	
Germany-*Kreditanstalt für Wiederaufbau* (KfW)	43.36
Japan Bank for International Cooperation (JBIC)	35.00
Norwegian Agency for Development Cooperation (NORAD)	1.00
Swedish International Development Cooperation Agency (SIDA)	5.77
U.S. Agency for International Development (USAID)	4.30
Subtotal	**89.43**
COFABs[2]	
Canadian International Development Agency (CIDA)	18.79
U.K. Department for International Development (DFID)	0.37
European Commission (EC)	16.12
Finland	0.05
Private Sector	0.29
Swiss State Secretariat for Economic Affairs (SECO)	8.70
Subtotal	**44.32**
TOTAL COFINANCING IN 2006	**$3,641.05**

[1] This list represents funds committed by the donor in the year. Agreements might still be under negotiation.
[2] Grant cofinancing contributions administered by the IDB.

Institutional Aspects

EL SALVADOR • CONDUSAL, a small cable-manufacturing company, implemented international quality standards.

GUATEMALA • Workers build shoulders on the road from Guatemala City to Antigua, which was repaved to handle increased traffic.

INSTITUTIONAL ASPECTS

BOARD OF GOVERNORS

The highest authority of the Bank is vested in the Board of Governors, composed of representatives of all member countries. Governors are usually ministers of the economy or finance, presidents of central banks or other officials of comparable rank.

The Forty-Seventh Annual Meeting took place in Belo Horizonte, Brazil, on April 3–5, 2006. At that time, the Board of Governors approved the financial statements of the Ordinary Capital, the Fund for Special Operations and the Intermediate Financing Facility for 2005, and selected Ernst & Young LLP to carry out the external audits for the 2006 fiscal year.

In addition, the Board of Governors assigned the Intermediate Financing Facility an aggregate amount equivalent to $61 million in convertible currency from the General Reserve of the Fund for Special Operations. It also approved an expansion of the scope of authority for Bank financing without sovereign guarantees to all eligible project entities in all sectors, subject to an exclusion list. Lastly, the Board of Governors resolved to hold the Fiftieth Annual Meeting in Medellín, Colombia, in 2009.

Prior to the inaugural session of the Annual Meeting, a Special Meeting of the Governors was held in Belo Horizonte, at which IDB President Luis Alberto Moreno, attending his first Annual Meeting as president, presented his vision for the IDB and discussed the issues of debt relief and the resources of the Fund for Special Operations.

Two other meetings were held before the inaugural session. The Committee of the Board of Governors held its Ninetieth Meeting, at which it considered the proposal to expand the scope of Bank financing without sovereign

TRINIDAD AND TOBAGO • Housing is one of six priority areas for the IDB under its Opportunities for the Majority initiative.

guarantees; and a joint meeting of the Committees of the Boards of Governors of the IDB and IIC was held to discuss the IDB Group and the private sector.

The Committee of the Board of Governors later held its Ninety-first meeting on July 17 and its Ninety-second meeting on November 17, both in Washington, D.C., to discuss debt relief and the concessional resources at the IDB.

At its last meeting, the Committee recommended that a proposed resolution on the "Agreement on the Bank's Concessional Resources" be submitted to the Board of Governors through the procedure of taking a vote without calling a meeting. The resolution was considered to have been adopted on December 21, 2006.

BOARD OF EXECUTIVE DIRECTORS

The IDB has 14 Executive Directors who represent the Bank's 47 member countries. Directors serve full time for a period of three years. In 2006, the Board of Executive Directors approved the loan and technical cooperation operations detailed in the section of this report on the year's lending. The principal corporate issues resolved by the Board are described below.

The *Audit Committee* oversees the Bank's financial reporting, risk management and internal controls, internal and external auditing, and institutional integrity. During the year, the committee considered the work of the external auditors on the Bank's annual financial statements and reviewed the Bank's quarterly financial statements. The committee also reviewed documentation on the Bank's integrity system, and a report on the framework for combating fraud and corruption in the activities financed by the IDB. The committee discussed the selection of the Auditor General and the appointment of external auditors, and reviewed quarterly reports on Bank progress toward COSO compliance with standards for internal controls on financial reporting set by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

The *Budget and Financial Policies Committee* reviews the Bank's administrative and capital budgets and financial policy issues. In 2006 it discussed the Fund for the Financing of Technical Cooperation for Initiatives for Regional Infrastructure Integration; an initiative to support country studies and improve and expand Bank loan operations; the Infrastructure Project Preparation Fund (InfraFund); and the Fund for the Financing of Disaster Prevention.

The committee's consideration of the 2007 budget led to a consensus on the Board to approve the administrative and capital budgets and adopt a framework for the realignment process, whereby management would submit a 2007 annual budget based on the Bank's current structure, with zero real growth and no change in headcount ceilings (approved in 2006) and a realignment budget. The Directors also underscored the importance of making strides towards a results-based administrative budget, with clear indicators for monitoring execution, which would lay the foundation for implementing a multiyear budget in 2008. The committee also discussed the Bank's financial outlook for the period 2006–2010; new Ordinary Capital loan charges for 2006 and operations for use of equity over the 38 percent Total Equity to Loan Ratio; the second activity report on the Development Effectiveness Program (PRODEV) and a request for reallocation of resources; the IDB borrowing program for 2006; and new sanctions procedures.

The *Organization, Human Resources and Board Matters Committee* deals with organizational issues related to

BOX 14 • IDB REALIGNS TO IMPROVE EFFECTIVENESS

The IDB's Board of Executive Directors approved a realignment of the IDB's organization in December 2006 in order to respond more efficiently to the challenges of development in Latin America and the Caribbean. The purpose of the overhaul is to enhance the effectiveness of the Bank so that it can better respond to these challenges.

To this end, the IDB will deepen its country focus and sector expertise and renew its emphasis on risk management and attainment of measurable results. The idea is to bring the Bank closer to the countries, and above all to make it an agent of real change in the lives of people in Latin America and the Caribbean.

In addition to the logistical aspects, the success of the new organization will depend to a great extent on changing the Bank's institutional culture. The realignment is designed to increase the Bank's responsiveness by strengthening its strategic and technical capacity and organizing its activities under four vice presidencies: Vice President for Countries; Vice President for Sectors and Knowledge; Vice President for Private Sector and Nonsovereign Guaranteed Operations; and Vice President for Finance and Administration. These vice presidents will report to the president and to the executive vice president of the Bank.

Among the strategic areas in which the Bank's knowledge and technical expertise will be deepened are those assigned priority under the Opportunities for the Majority initiative, which includes developing policies, strategies and programs that provide greater access to housing, financial services, basic infrastructure, jobs, information and communication technologies, and further the identification and registration of the region's undocumented population. Achieving the Millennium Development Goals also remains a priority. The IDB can help the countries implement effective social policies that are conducive to poverty reduction, human capital development and better living conditions for the neediest segments of the population.

The realignment will also help the IDB focus on supporting development of science and technology and their application in productive processes, to raise productivity and promote innovation. It will help the Bank's work with countries to boost investment in infrastructure to make the region more competitive and enhance its physical and energy interconnection.

The new structure will also promote private sector development and job creation by implementing the Bank's expanded mandate to lend to private initiatives in all sectors and to state-owned enterprises and subnational entities without sovereign guarantees.

IDB management is to submit an implementation plan to the Board of Executive Directors for the realignment in early 2007.

HONDURAS • A nurse feeds a preterm baby in Comayagua.

Board management, adjustments in the structure of the Bank, human resources, the Independent Investigation Mechanism and the Bank's Annual Meeting. In 2006, the committee discussed the realignment of the Bank to better serve the needs of the borrowing member countries, including a new basic organizational structure which would increase the organization's efficiency and adaptability to better respond to the countries' needs (see Box 14 on the realignment). The realignment was approved by the Board in December.

The committee also considered a proposal to amend the Board's regulations to reduce the advance distribution period for loan and policy documents from three weeks to two weeks, in order to expedite consideration; recommended the appointment of two members of the Administrative Tribunal to the Board of Executive Directors; and discussed one Independent Investigation Mechanism case (Provincial Route 28 in Argentina), endorsing the consultant's recommendations not to convene a full panel, in recognition of management's efforts to resolve outstanding issues.

The *Policy and Evaluation Committee* considers the policies and strategies that guide Bank operations in the region and the instruments used to implement them, and oversees the Office of Evaluation and Oversight. During the year, the

BELIZE • Drainage works in Belize City help prevent damage from hurricanes.

BOX 15 • IDB OFFICES IN EUROPE AND JAPAN STRENGTHEN PARTNERSHIPS

Office in Europe

The IDB Office in Europe works to strengthen strategic partnerships, dialogue and cooperation between the Bank and countries in Europe and Latin America and the Caribbean. In addition to forging closer ties to the Bank with its 16 European member countries and Israel, the office, which is located in Paris, is also active in expanding its cooperation with European Union institutions and other international organizations based in Europe.

These include the Organisation for Economic Cooperation and Development, World Trade Organization, Secretariat of Ibero-American Cooperation, United Nations Office on Drugs and Crime, United Nations Conference on Trade and Development, United Nations Educational, Scientific and Cultural Organization, and *Agence française de développement* (French Development Agency). The key mission of the Paris office is to promote greater awareness of the IDB by increasing its visibility, reinforcing cooperation with European institutions in various areas and facilitating the exchange of experiences between Europe and Latin America.

The office's core activities in 2006 focused on five main areas: interagency coordination, Euro-Latin networks, the private sector, social programs and outreach. For example, the office created a network of private sector liaison officers in major European business organizations. The office continued to expand its activities through the Governance for Development Network, Network on Integration and Trade, and Competition Forum, generating interest from academics, researchers and policymakers.

During the year, the office also strengthened its participation in the Steering Committee of EUROsociAL, the European Union's main social program in Latin America, which works to build social cohesion through public policy in education, health, justice, taxation and employment.

The Office in Europe organized over 50 events during the year, such as conferences, one-day forums on Latin American issues, workshops and business outreach seminars in various European capitals. It participated in another 50 international meetings on behalf of the Bank.

committee conducted policy discussions on a number of key issues, such as the Environment and Safeguards Compliance Policy, the Policy on Indigenous Peoples and the Strategy for Indigenous Development. Several initiatives were also considered, including a proposal to expand the scope of the Bank's financing without sovereign guarantees under the 10 percent authority (approved by the Board of Governors at the Annual Meeting in Belo Horizonte); extension of the sector facility framework; modifications in performance-driven loans; and a proposal for partial credit guarantees in local currency without sovereign guarantees. These new policies were approved by the Board.

Office in Japan

The IDB's Office in Japan works to build development partnerships with the Bank's member countries in Latin America and the Caribbean, and with Japan, the Republic of Korea and other East Asian countries. During 2006, it engaged in outreach and dissemination activities, through seminars, workshops, roundtables, business consultations and publications.

For example, it conducted information seminars and meetings with Japanese and Korean companies interested in doing business with member countries in Latin America and the Caribbean. It also offered investment and trade promotion seminars in connection with the visits to Japan and Korea of dignitaries, high-ranking officers and business leaders from the region.

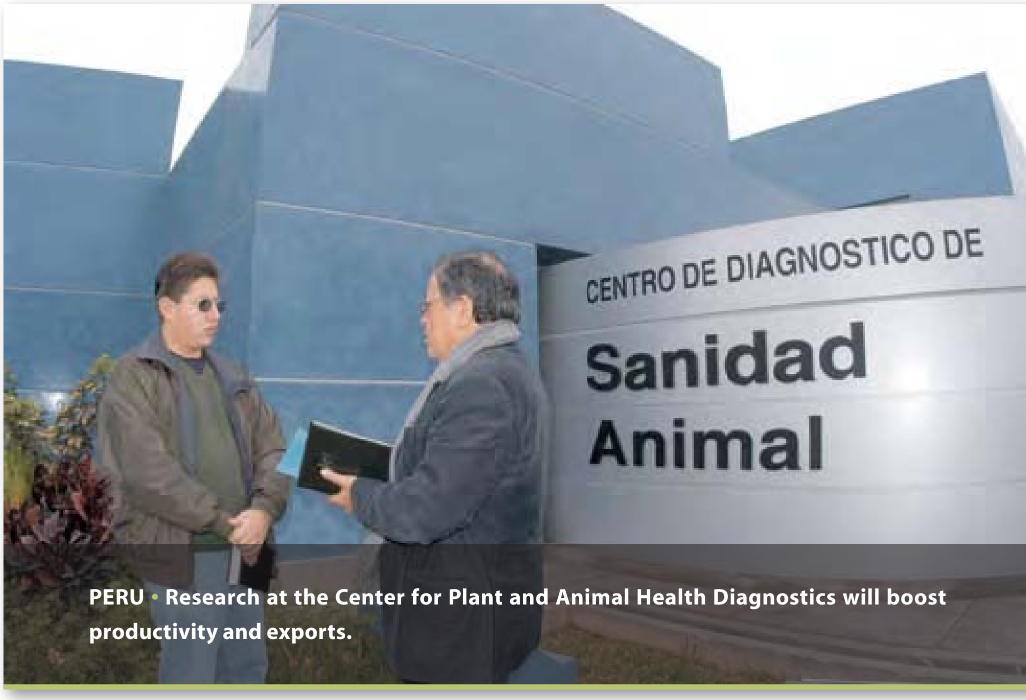
With the participation of President Moreno and a group of business leaders from Japan and Latin America, the office organized, with the Japan Bank for International Cooperation, a private sector forum on the business environment in Latin America and the Caribbean and opportunities available to Asian investors in the region. It supported a similar event in Korea jointly with private sector organizations.

In the context of the Forum for East Asia–Latin America Cooperation and the Asia-Pacific Economic Cooperation, the Office in Japan supported events on regional cooperation, integration and trade. Under the Bank's partnership agreement with the Asian Development Bank, the office implemented activities jointly with that organization in Japan and the Philippines, and in Korea, in conjunction with the Asian Development Bank Institute, it held the Third Annual Conference of the Latin America/Caribbean Asia/Pacific Economics and Business Association. The office in Japan participated in business cooperation missions to Chile and Argentina organized by the Japan/Tokyo Chamber of Commerce and Industry and in a business symposium for Okinawan descendants worldwide.

To mobilize resources for Bank projects, the office held meetings with the Japan Bank for International Cooperation and the Japan International Cooperation Agency, as well as consultations with Japan's Ministry of Finance and other relevant public and private institutions in Japan and Korea.

The committee also considered evaluation reports produced by the Office of Evaluation and Oversight; the office's annual report and work program; ex post project evaluations; thematic evaluations; and an assessment of project completion reports. It discussed the 2005 Annual Report on Portfolio Management, Performance and Results and other progress reports, and a report on the IDB group and the private sector.

The *Programming Committee* considers country and regional programming documents, country strategies and country program evaluations; reviews progress reports on the Bank's lending, technical cooperation and nonfinancial



PERU • Research at the Center for Plant and Animal Health Diagnostics will boost productivity and exports.

product pipelines; and evaluates guidelines for the allocation of concessional resources. In 2006, the committee reviewed the country strategies for Barbados, Jamaica and Uruguay; the mid-term assessment of the IDB country strategy with Argentina; and country strategy updates. In its discussions, it focused on the quality of targets and indicators to enhance the development effectiveness of country strategies.

The committee discussed and recommended approval of allocations for the Fund for Special Operations and Intermediate Financing Facility. Also discussed were reports on the "Medium-Term Action Plan: Overview of Progress in 2005 and the Way Forward"; "The New Lending Framework: Overview of Implementation in 2005"; the 2005 Call for Proposals under the "Initiative for the Promotion of Regional Public Goods"; and the Evaluation of the IDB Action Plan for Private Sector Development in C- and D-group countries.

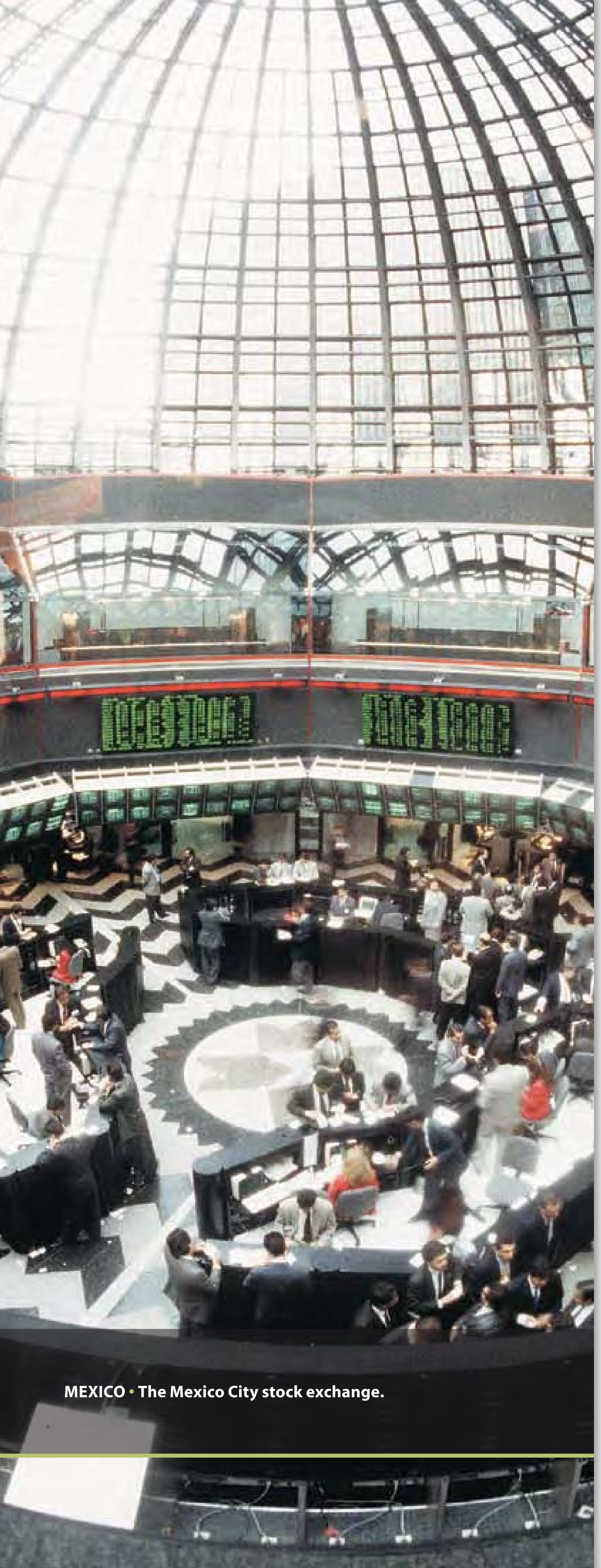
For information on the consolidated administrative expenses of the IDB, see table XV in the CD-Rom.

ADMINISTRATION

Management completed the 100-position reduction in the Bank's headcount for the period 2004–2006 mandated by the Board of Executive Directors. At year-end 2006, Bank staff funded by the administrative budget, excluding the Board of Executive Directors, the Office of Evaluation and Oversight and the Multilateral Investment Fund, totaled 1,824, of whom 1,417 were professionals and 407 administrative staff. Headquarters staff numbered 1,306 and Country Office personnel 518. There were 574 professional women, representing 40.5 percent of all professional staff.

Financial Highlights

GUATEMALA • Miguel Angel Morales ("Manuel") runs the cattle operation for a cooperative of ex-combatants in the Petén region.



MEXICO • The Mexico City stock exchange.

FINANCIAL HIGHLIGHTS

ORDINARY CAPITAL

During 2006, the Bank approved 90 loans amounting to $5.4 billion from the Ordinary Capital resources as compared to 72 loans for $6.4 billion in 2005. The decrease in the amount of loan approvals was mostly due to a decrease in investment lending that was partially offset by an increase in policy-based and non-sovereign-guaranteed lending. Also, disbursements totaled $6.1 billion, higher than the $4.9 billion disbursed in 2005. Undisbursed loans decreased to $16.1 billion in 2006 from $17 billion in 2005.

The Bank also approved two non-trade-related guarantees without sovereign counter-guarantees for $180 million in 2006 as compared to one guarantee for $28 million in 2005. In addition, the Bank approved its first partial credit guarantee operation with a government counter-guarantee for $60 million. Ten trade finance guarantee lines of credit totaling $133 million were authorized under the Trade Finance Facilitation Program (compared to 10 and $270 million, respectively, in 2005), and an existing line was increased by $20 million.

Since the Bank's inception, there have been no write-offs in the sovereign-guaranteed loan portfolio, which, as of December 31, 2006, represented over 97 percent of the $45.9 billion in loans outstanding. As of that date, all loans were performing, except for certain non-sovereign-guaranteed loans totaling $66 million (2005—$196 million), which were classified as impaired, and were in nonaccrual status. The allowances for loan and guarantee losses amounted to $104 million compared to $188 million in 2005. The decrease was mainly

GUATEMALA • *Jatropha curcas,* known locally as the piñón, holds great potential as a biodiesel fuel.

due to higher than expected impaired loan collections, as well as write-offs of $42 million.

The Bank issued bonds for a total face amount of $5.4 billion equivalent (2005—$4.9 billion) and proceeds of $5.3 billion (2005—$4.9 billion) with an average life of 6.5 years (2005—6.3 years). Borrowings raised in any given year are used for general operations, including loan disbursements and refinancing of maturing debt. The Bank launched two global benchmark $1 billion bonds in 2006 with five-year and 10-year maturities, and transacted bonds denominated in Australian dollars, Canadian dollars, New Zealand dollars, South African rand and United States dollars.

In 2006, the Bank also issued bonds denominated in borrowing member country currencies totaling $526 million (2005—$496 million), comprised of the following currencies: Mexican pesos $406 million and Peruvian new soles $120 million (2005—Chilean pesos $66 million, Colombian pesos $72 million, and Mexican pesos $358 million). These included the first-ever supranational structured bond denominated in Mexican pesos and the Bank's first bonds denominated in Peruvian new soles, one of which was the largest Peruvian new soles bond ever issued by a foreign entity. Bonds denominated in currencies from borrowing member countries are on a cost-effective basis for the Bank, and their issuance contributes, in part, to the development of local capital markets and expands effective foreign demand for local currencies.

Figure 10 shows the Bank's debt issues during 2006 by currency. All non-United States dollar issues were initially swapped to U.S. dollars. Tables VII and VIII below provide more detail on these borrowings as well as outstanding borrowings by currency before swaps as of December 31, 2006.

The Bank continued to be rated AAA by the major credit agencies in 2006, as it has been since it was first rated.

Operating Income was $627 million in 2006 compared with $712 million in 2005. The decrease was largely due to a reduction in income generated by the loan portfolio and an increase in net non-interest expense, partially offset by an increase in the release of provision for loan and guarantee losses. Against a background of steady growth of the Total Equity to Loans Ratio (TELR) in recent years, which surpassed the desired level of 38 percent during 2006, the Bank charged lending spreads of 0.10 percent and 0.15 percent for the first and second semesters, respectively, a commission of 0.10 percent and no supervision and inspection fee, lower than standard loan charges.

FIGURE 10. BORROWINGS ISSUED IN 2006, BEFORE SWAPS

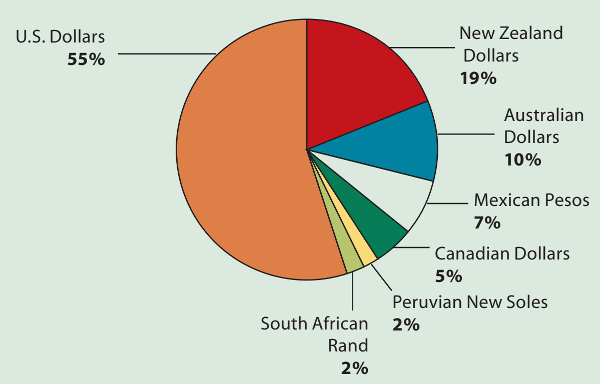


TABLE VII • BORROWINGS,[1] FISCAL YEAR 2006
(Amounts in millions)

Type	Issue	Amount	Amount (US$ equiv.)
Australian dollars	4.80%, due 2009	63	$ 47
	5.43%, due 2009	143	109
	5.75%, due 2010	100	77
	5.75%, due 2011	100	77
	6.00%, due 2011	300	228
Canadian dollars	4.40%, due 2026	300	261
Mexican pesos	8.30%, due 2010	350	31
	7.60%, due 2011	300	29
	8.25%, due 2011	200	18
	7.80%, due 2011	120	11
	7.50%, due 2011	400	36
	7.65%, due 2013	140	13
	7.50%, due 2013	330	30
	8.00%, due 2016	2,500	238
New Zealand dollars	5.67%, due 2008	761	491
	6.00%, due 2008	419	266
	6.13%, due 2011	100	62
	6.25%, due 2011	100	64
	6.26%, due 2016	200	122
Peruvian new soles	6.09%, due 2008	65	20
	6.63%, due 2017	324	100
South African rand	7.74%, due 2010	50	7
	7.25%, due 2011	300	41
	8.50%, due 2016	250	36
United States dollars	5.25%, due 2008	500	500
	4.15%, due 2009	50	50
	4.60%, due 2009	230	230
	5.00%, due 2011	1,000	1,000
	5.13%, due 2016	1,000	1,000
	0.00%, due 2026	225	225
TOTAL BORROWINGS			**$5,419**

[1] Medium- and long-term borrowings at face value, before swaps.

Since the adoption of the Bank's capital adequacy policy in 2003, the Bank's measure of risk-based capital adequacy, the TELR, has steadily increased as a result of an increase in the equity base and a reduction in loan levels, mostly due to loan prepayments. By the end of the year, the TELR had reached a level of 40.8 percent. Management has presented to the Board of Executive Directors a document on options for the use of equity exceeding the 38 percent upper bound of the TELR. The Board of Executive Directors has the matter under consultation.

TABLE VIII • OUTSTANDING BORROWINGS BY CURRENCY AS OF DECEMBER 31, 2006
(In millions of U.S. dollars)

Currency[1]	Amount
Australian dollars	$ 4,427
Brazilian reais	357
British pounds sterling	2,348
Canadian dollars	2,917
Chilean pesos	71
Colombian pesos	96
Euro	3,489
Hong Kong dollars	97
Icelandic krónur	70
Japanese yen	2,690
Mexican pesos	1,029
New Taiwan dollars	123
New Zealand dollars	2,736
Peruvian new soles	122
South African rand	492
Swiss francs	821
United States dollars	24,511
TOTAL	**$46,396**

[1] Medium- and long-term borrowings at face value, before swaps.

GUYANA • Lisa Simbo, a student at Rama Krishna Primary School in Georgetown, listens in during her computer class.

Significant Developments in 2006

In December 2006, the Board of Executive Directors approved changes to the Bank's basic organization directed at improving the Bank's operational efficiency and capacity to fulfill its fundamental purpose. The changes include the creation of three new Vice President positions: Vice President for Countries, Vice President for Sectors and Knowledge, and Vice President for Private Sector and Non-Sovereign-Guaranteed Operations. The realignment is subject to further approval of implementation measures by the Board of Executive Directors (see Box 14).

The implementation of the Local Currency Facility was rolled out in 2006. The Board of Executive Directors approved six new operations to entities in Brazil, Chile, Mexico and Peru. The Bank also made three additional disbursements in Mexican pesos of $19 million each under a loan approved in 2001.

In April 2006, the Board of Governors authorized the Board of Executive Directors to expand the scope of authority regarding private sector financing without sovereign guarantees under the 10 percent limit: (a) to encompass projects in all sectors, subject to an exclusion list, thereby eliminating restrictions previously limiting such financing only to infrastructure, capital markets and trade finance operations; and (b) to include sub-sovereigns. In August 2006, the Board of Executive Directors approved an integrated business plan and revised operational guidelines for operations without sovereign guarantees, making this authorization effective.

TABLE IX • STATEMENT OF LOANS OUTSTANDING AS OF DECEMBER 31, 2006

(In millions of U.S. dollars)

Member in whose territory loans have been made	Ordinary Capital: Public Sector	Ordinary Capital: Private Sector	Ordinary Capital: Subtotal	Fund for Special Operations[1]	Total
Argentina	$ 8,465	$ 52	$ 8,517	$ 109	$ 8,626
Bahamas	74	—	74	—	74
Barbados	141	—	141	12	153
Belize	80	—	80	—	80
Bolivia	233	93	326	955	1,281
Brazil	11,743	346	12,089	281	12,370
Chile	550	12	562	—	562
Colombia	4,294	—	4,294	121	4,415
Costa Rica	535	11	546	71	617
Dominican Republic	1,067	—	1,067	353	1,420
Ecuador	1,326	22	1,348	504	1,852
El Salvador	1,128	—	1,128	450	1,578
Guatemala	959	—	959	331	1,290
Guyana	6	—	6	455	461
Haiti	—	—	—	609	609
Honduras	104	—	104	1,264	1,368
Jamaica	565	30	595	43	638
Mexico	3,999	236	4,235	17	4,252
Nicaragua	84	7	91	1,060	1,151
Panama	842	—	842	42	884
Paraguay	658	—	658	301	959
Peru	3,622	127	3,749	56	3,805
Suriname	49	—	49	1	50
Trinidad and Tobago	377	—	377	8	385
Uruguay	1,837	10	1,847	19	1,866
Venezuela	1,574	—	1,574	—	1,574
Regional	531	143	674	53	727
TOTAL	**$44,843**	**$1,089**	**$45,932**	**$ 7,115**	**$53,047**

[1] Excludes loan participations sold to the Social Progress Trust Fund for a total of $40 million, including $3 million to Bolivia, $8 million to the Dominican Republic, $4 million to Ecuador, $3 million to El Salvador, $8 million to Guatemala, $8 million to Honduras, $4 million to Nicaragua, $1 million to Panama, and $1 million to Paraguay.

In October 2006, the Bank commenced an External Managers Program to manage up to 10 percent of its liquid investment portfolio under the Bank's overall Investment Guidelines. At December 31, 2006, the Bank had investments of $407 million managed by two external financial firms.

The Bank implemented the Committee of Sponsoring Organizations of the Treadway Commission (COSO) Internal Control-Integrated Framework for its financial reporting, and established an annual process for management to report on the effectiveness of the internal control over financial reporting, and for the external auditors to attest to the accuracy of management's assessment and as to the effectiveness of internal control over financial reporting. Management's first assessment report and the auditors' attestation were performed for financial information as of December 31, 2006, and are included in the Ordinary Capital's financial statements.

FUND FOR SPECIAL OPERATIONS

VENEZUELA • Government employees learn to use new systems designed to improve efficiency.

In 2006, there were 23 loans approved amounting to $602 million from the Bank's concessional window, the FSO, as compared to 20 loans approved amounting to $410 million in 2005. In addition, the FSO approved its first ever guarantee operation of $2.5 million. As of December 31, 2006, the loan portfolio amounted to $7.1 billion (2005 – $6.9 billion) and was fully performing. FSO operations generated income over expenses, before technical cooperation expense and Heavily Indebted Poor Countries (HIPC) debt relief, of $119 million compared to $101 million in 2005.

The amount of $61 million (2005—$62 million) was allocated from the FSO to the IFF for its standard operations, for the HIPC Initiative, and in connection with the agreement on concessional resources approved by the Board of Governors in 1999.

During 2006, the Bank continued to deliver debt relief to Bolivia, Guyana, Honduras and Nicaragua, according to its commitments under the Original and the Enhanced HIPC Initiatives. As originally designed, the Bank is financing its participation in these initiatives through local currency conversions from borrower member countries, contributions from the HIPC Trust Fund received from nonborrowing member countries and FSO internal resources.

Through 2006, the nominal amount of debt relief delivered as part of the Original and Enhanced Initiatives was $735 million: $327 million for Bolivia, $117 million for Guyana, $98 million for Honduras and $193 million for Nicaragua. All borrowing member countries eligible for HIPC debt relief, as of December 31, 2006, have reached completion point under the Enhanced Initiative; as a result, the Bank wrote off FSO loans of $505 million, $64 million, $85 million and $409 million for Bolivia, Guyana, Honduras and Nicaragua, respectively, in prior years. At the time of write-off, these figures represented the estimated principal portion of debt relief remaining to be provided from FSO internal resources under the Enhanced Initiative, net of debt relief previously delivered. For the Original Initiative, loan write-offs of $177 million were recognized in 1998.

Significant Developments in 2006

In January 2007, the Board of Governors approved debt relief for Haiti under the Enhanced HIPC Initiative. Haiti, which has reached decision point, is expected to receive debt relief under this initiative in the amount of $60.4 million in net present value terms.

The World Bank's International Development Agency, the International Monetary Fund and the African Development Fund have approved their participation in the Multilateral Debt Relief Initiative (MDRI) to provide additional debt relief to HIPC countries. Although the MDRI does not include the Bank, the Bank's Board of Governors has supported the principle of furthering FSO debt relief for HIPC-eligible countries in Latin America and the Caribbean.

In December 2006, the Board of Governors approved a structure including 100 percent relief of eligible FSO debt for Bolivia, Guyana, Haiti, Honduras and Nicaragua, effective January 1, 2007 (Haiti would qualify once it reaches completion point for the Enhanced HIPC Initiative), as well as (i) the continuance of the access to concessional

TABLE X • SUBSCRIPTIONS TO CAPITAL STOCK, CONTRIBUTION QUOTAS AND VOTING POWER AS OF DECEMBER 31, 2006

(In millions of U.S. dollars)

Member countries	Ordinary Capital Subscribed Capital Stock			Percent of Total Number of Votes[1,3]	FSO Contribution Quotas
	Paid-in	Callable	Total		
Regional Developing Members					
Argentina	$ 465.1	$ 10,393.8	$ 10,858.9	10.752	$ 511.7
Bahamas	11.6	198.3	209.9	0.209	10.6
Barbados	5.6	124.3	129.9	0.130	1.8
Belize	7.2	103.5	110.7	0.111	7.6
Bolivia	37.3	834.4	871.7	0.865	48.7
Brazil	465.1	10,393.8	10,858.9	10.752	544.4
Chile	127.7	2,853.9	2,981.6	2.953	157.7
Colombia	127.7	2,853.9	2,981.6	2.953	153.7
Costa Rica	18.7	417.1	435.7	0.433	23.4
Dominican Republic	24.9	556.8	581.7	0.577	33.9
Ecuador	24.9	556.8	581.7	0.577	30.3
El Salvador	18.7	417.1	435.7	0.433	21.4
Guatemala	24.9	556.8	581.7	0.577	32.8
Guyana	7.8	153.8	161.6	0.162	8.3
Haiti	18.7	417.1	435.7	0.433	21.8
Honduras	18.7	417.1	435.7	0.433	26.5
Jamaica	24.9	556.8	581.7	0.577	28.8
Mexico	299.0	6,681.3	6,980.3	6.912	329.0
Nicaragua	18.7	417.1	435.7	0.433	24.2
Panama	18.7	417.1	435.7	0.433	25.4
Paraguay	18.7	417.1	435.7	0.433	27.9
Peru	62.3	1,390.7	1,453.0	1.440	79.8
Suriname	5.7	82.9	88.6	0.089	6.3
Trinidad and Tobago	18.7	417.1	435.7	0.433	20.9
Uruguay	49.9	1,114.3	1,164.2	1.154	55.9
Venezuela	249.3	5,568.5	5,817.8	5.761	315.3
Total regional developing members	**2,170.5**	**48,311.4**	**50,481.1**	**50.016**	**2,548.1**
Canada	**173.7**	**3,866.2**	**4,039.9**	**4.001**	**316.8**
United States	**1,303.0**	**29,006.7**	**30,309.7**	**30.007**	**4,839.0**
Nonregional Members					
Austria	6.9	153.7	160.6	0.161	20.6
Belgium	14.2	316.8	331.0	0.329	46.8
Croatia	2.1	46.4	48.5	0.050	6.0
Denmark	7.3	163.4	170.8	0.171	21.9
Finland	6.9	153.7	160.6	0.161	19.6
France	82.3	1,831.4	1,913.7	1.896	241.9
Germany	82.3	1,831.4	1,913.7	1.896	241.9
Israel	6.8	151.5	158.3	0.158	19.0
Italy	82.3	1,831.4	1,913.7	1.896	229.3
Japan	217.1	4,833.2	5,050.3	5.001	576.5
Korea, Republic of	0.1	2.1	2.2	0.004	–
Netherlands	14.6	325.6	340.3	0.338	40.5
Norway	7.3	163.4	170.8	0.171	20.6
Portugal	2.3	51.7	54.0	0.055	7.8
Slovenia	1.3	28.1	29.4	0.031	3.4
Spain	82.3	1,831.4	1,913.7	1.896	227.6
Sweden	14.1	314.8	328.9	0.327	41.1
Switzerland	20.4	454.2	474.7	0.472	67.5
United Kingdom	41.8	929.9	971.7	0.964	183.6
Total nonregional members	**692.4**	**15,414.3**	**16,106.9**	**15.976**	**2,015.6**
Total before unallocated amount	**4,339.4**	**96,598.5**	**100,937.9**		**9,719.5**
Unallocated[2]	0.9	14.8	15.7		5.4
GRAND TOTAL	**$ 4,340**	**$ 96,613**	**$ 100,953**	**100.000**	**$ 9,725**

[1] Data are rounded; detail may not add to subtotals and grand total because of rounding.
[2] Represents the remaining shares and contribution quotas of the former Socialist Federal Republic of Yugoslavia.
[3] Each member country's voting power is the same in making decisions concerning the operations of the Ordinary Capital and the FSO. Except where otherwise expressly provided in the Agreement Establishing the Bank, all matters are decided by a majority of the total voting power of the member countries.

resources for FSO countries (other than Haiti) via a blending of loans from the FSO and the Ordinary Capital ("parallel loans"), (ii) Haiti's access to an appropriate mix of loans and/or grants with adequate levels of concessionality, (iii) the IFF's extension to 2015 via a blending of FSO resources and Ordinary Capital loans, and (iv) annual nonreimbursable technical assistance of $30 million.

To implement this structure for further debt relief, in January 2007 the Committee of the Board of Governors agreed to submit a proposal to the Board of Governors identifying as such eligible FSO debt the approximate principal amount of $3.4 billion in outstanding FSO loan balances as of December 31, 2004, subject to the Board of Executive Directors' approval of a reform proposal presented by management on the future operations of the FSO. If approved, inter alia, the FSO would bear a smaller percentage of the administrative expenses of the Bank currently allocated between the Ordinary Capital and the FSO; and countries eligible for IFF subsidies would continue to receive concessional resources for new loans through 2015, in the form of parallel loans rather than a reduction in the interest rate billed, and would still receive the reduction in interest rate billed for existing loans, even though FSO transfers to the IFF would not reoccur before 2014. A vote on the proposal is expected in the first quarter of 2007.

HAITI • A papaya farmer in Charrette sees big results after a new channel brought reliable irrigation.

Copies of the basic financial statements of the Ordinary Capital, the FSO and the IFF appear on pages 72–78. The full set of the financial statements, including the external auditors' opinions and the notes to the financial statements, are presented in the Management's Discussion and Analysis and Financial Statements section of this Annual Report.

ORDINARY CAPITAL
INTER-AMERICAN DEVELOPMENT BANK

BALANCE SHEET

Expressed in millions of United States dollars

	December 31,			
	2006		2005	
ASSETS				
Cash and investments				
Cash	$ 276		$ 223	
Investments				
Trading	12,278		10,183	
Held-to-maturity	3,543	$16,097	3,414	$13,820
Loans outstanding	45,932		48,135	
Allowance for loan losses	(90)	45,842	(175)	47,960
Accrued interest and other charges				
On investments	95		85	
On loans	594		587	
On swaps, net	25	714	73	745
Receivable from members				
Non-negotiable, non-interest-bearing demand obligations	361		370	
Amounts required to maintain value of currency holdings	57	418	73	443
Currency and interest rate swaps				
Investments—trading	2		3	
Loans	5		5	
Borrowings	1,880	1,887	1,596	1,604
Other assets				
Postretirement benefit assets	863		186	
Property, net	301		326	
Unamortized borrowing costs	196		218	
Miscellaneous	157	1,517	80	810
Total assets		$66,475		$65,382
LIABILITIES AND EQUITY				
Liabilities				
Borrowings				
Short-term	$ 658		$ 926	
Medium- and long-term	44,030	$44,688	44,167	$45,093
Currency and interest rate swaps				
Investments—trading	1		61	
Loans	9		10	
Borrowings	742	752	491	562
Payable for investment securities purchased		47		45
Amounts payable to maintain value of currency holdings		315		188
Accrued interest on borrowings		586		607
Accounts payable and accrued expenses		279		160
Total liabilities		46,667		46,655
Equity				
Capital stock				
Subscribed 8,368,563 shares	100,953		100,953	
Less callable portion	(96,613)		(96,613)	
Paid-in capital stock	4,340		4,340	
Retained earnings	14,442		14,199	
Accumulated other comprehensive income	1,026	19,808	188	18,727
Total liabilities and equity		$66,475		$65,382

ORDINARY CAPITAL
INTER-AMERICAN DEVELOPMENT BANK

STATEMENT OF INCOME AND RETAINED EARNINGS

Expressed in millions of United States dollars

	Years ended December 31, 2006	2005	2004
Income			
Loans			
Interest	**$ 2,435**	$ 2,368	$ 2,446
Other loan income	**31**	45	52
	2,466	2,413	2,498
Investments	**619**	403	288
Other	**12**	14	11
Total income	**3,097**	2,830	2,797
Expenses			
Borrowing expenses			
Interest, after swaps	**2,015**	1,678	1,526
Amortization of borrowing costs	**55**	55	46
	2,070	1,733	1,572
(Credit) provision for loan and guarantee losses	**(48)**	(14)	21
Administrative expenses	**414**	387	342
Special programs	**34**	12	—
Total expenses	**2,470**	2,118	1,935
Income before SFAS 133 and currency transaction adjustments	**627**	712	862
Effects of SFAS 133 and currency transaction adjustments	**(384)**	50	314
Net income	**243**	762	1,176
Allocation to the Fund for Special Operations	**—**	—	(27)
Addition to Retained earnings for the year	**243**	762	1,149
Retained earnings, beginning of year	**14,199**	13,437	12,288
Retained earnings, end of year	**$14,442**	$14,199	$13,437

STATEMENT OF COMPREHENSIVE INCOME

Expressed in millions of United States dollars

	Years ended December 31, 2006	2005	2004
Net income	**$243**	$ 762	$1,176
Other comprehensive income			
Translation adjustments	**149**	(554)	239
Reclassification to income—cash flow hedges	**8**	8	11
Total other comprehensive income (loss)	**157**	(546)	250
Comprehensive income	**$400**	$ 216	$1,426

ORDINARY CAPITAL
INTER-AMERICAN DEVELOPMENT BANK

STATEMENT OF CASH FLOWS

Expressed in millions of United States dollars

	Years ended December 31,		
	2006	**2005**	**2004**
Cash flows from lending and investing activities			
Lending:			
Loan disbursements (net of participations)	**$ (6,088)**	$ (4,899)	$ (3,768)
Loan collections (net of participations)	**8,615**	5,224	5,199
Loan recoveries	**3**	9	—
Net cash provided by lending activities	**2,530**	334	1,431
Gross purchases of held-to-maturity investments	**(2,049)**	(2,392)	(4,448)
Gross proceeds from maturities of held-to-maturity investments	**2,056**	2,531	4,420
Purchase of property	**(15)**	(24)	(34)
Miscellaneous assets and liabilities	**7**	(6)	17
Net cash provided by lending and investing activities	**2,529**	443	1,386
Cash flows from financing activities			
Medium- and long-term borrowings:			
Proceeds from issuance	**5,276**	5,039	4,519
Repayments	**(6,510)**	(5,711)	(7,798)
Short-term borrowings:			
Proceeds from issuance	**10,276**	8,602	6,059
Repayments	**(10,559)**	(7,969)	(7,325)
Collections of receivable from members	**12**	26	35
Net cash used in financing activities	**(1,505)**	(13)	(4,510)
Cash flows from operating activities			
Gross purchases of trading investments	**(20,468)**	(14,670)	(15,901)
Gross proceeds from sale or maturity of trading investments	**18,672**	13,329	17,977
Loan income collections	**2,457**	2,405	2,426
Interest and other costs of borrowings, after swaps	**(1,857)**	(1,544)	(1,412)
Income from investments	**588**	395	273
Other income	**13**	14	10
Administrative expenses	**(367)**	(335)	(352)
Special programs	**(7)**	(1)	—
Net cash (used in) provided by operating activities	**(969)**	(407)	3,021
Cash allocation to the Fund for Special Operations	**—**	—	(27)
Effect of exchange rate fluctuations on cash	**(2)**	(10)	(7)
Net increase (decrease) in Cash	**53**	13	(137)
Cash, beginning of year	**223**	210	347
Cash, end of year	**$ 276**	$ 223	$ 210

FUND FOR SPECIAL OPERATIONS
INTER-AMERICAN DEVELOPMENT BANK

SPECIAL PURPOSE STATEMENT OF ASSETS, LIABILITIES AND FUND BALANCE

Expressed in millions of United States dollars

	December 31,			
	2006		2005	
ASSETS				
Cash and investments				
Cash	**$ 389**		$ 378	
Investments	**1,203**	**$1,592**	1,182	$1,560
Loans outstanding		**7,115**		6,873
Accrued interest and other charges				
On investments	**—**		4	
On loans	**39**	**39**	38	42
Receivable from members				
Non-negotiable, non-interest-bearing demand obligations	**567**		628	
Amounts required to maintain value of currency holdings	**209**	**776**	272	900
Receivable for investment securities sold		**—**		4
Other assets		**8**		7
Total assets		**$9,530**		$9,386
LIABILITIES AND FUND BALANCE				
Liabilities				
Accounts payable and accrued expenses	**$ 6**		$ 11	
Undisbursed technical cooperation projects and other financings	**84**		94	
Amounts payable to maintain value of currency holdings	**300**	**$ 390**	240	$ 345
Fund balance				
Contribution quotas authorized and subscribed	**9,725**		9,671	
General reserve (deficit)	**(583)**		(627)	
Accumulated translation adjustments	**(2)**	**9,140**	(3)	9,041
Total liabilities and fund balance		**$9,530**		$9,386

FUND FOR SPECIAL OPERATIONS
INTER-AMERICAN DEVELOPMENT BANK

SPECIAL PURPOSE STATEMENT OF CHANGES IN GENERAL RESERVE (DEFICIT)

Expressed in millions of United States dollars

	Years ended December 31,		
	2006	**2005**	**2004**
Income			
Loans			
Interest	**$ 139**	$ 135	$ 131
Other loan income	**13**	14	14
	152	149	145
Investments	**60**	38	21
Total income	**212**	187	166
Expenses			
Administrative expenses	**93**	86	62
Total expenses	**93**	86	62
Excess of income over expenses before technical cooperation expense and HIPC debt relief	**119**	101	104
Technical cooperation expense	**19**	28	31
HIPC debt relief	**(5)**	76	486
Excess of income over expenses (expenses over income)	**105**	(3)	(413)
General reserve (deficit), beginning of year	**(627)**	(562)	(76)
Allocations to Intermediate Financing Facility Account	**(61)**	(62)	(73)
General reserve (deficit), end of year	**$(583)**	$(627)	$(562)

SPECIAL PURPOSE STATEMENT OF COMPREHENSIVE INCOME

Expressed in millions of United States dollars

	Years ended December 31,		
	2006	**2005**	**2004**
Excess of income over expenses (expenses over income)	**$105**	$ (3)	$(413)
Translation adjustments on assets and liabilities	**54**	(89)	57
Comprehensive income (loss)	**$159**	$(92)	$(356)

FUND FOR SPECIAL OPERATIONS
INTER-AMERICAN DEVELOPMENT BANK

SPECIAL PURPOSE STATEMENT OF CASH FLOWS

Expressed in millions of United States dollars

	Years ended December 31,		
	2006	2005	2004
Cash flows from lending activities			
Lending:			
Loan disbursements	**$ (398)**	$ (424)	$ (463)
Loan collections	**290**	301	294
Loan participations, net	**(2)**	(1)	—
Net cash used in lending activities	**(110)**	(124)	(169)
Cash flows from financing activities			
Collections of receivable from members	**101**	130	150
Net cash provided by financing activities	**101**	130	150
Cash flows from operating activities			
Gross purchases of investments	**(1,208)**	(2,269)	(2,527)
Gross proceeds from sale or maturity of investments	**1,233**	2,237	2,556
Loan income collections	**152**	146	136
Income from investments	**26**	38	19
Administrative expenses	**(99)**	(77)	(83)
Technical cooperation and other financings	**(29)**	(34)	(31)
Net cash provided by operating activities	**75**	41	70
Cash allocations to the Intermediate Financing Facility Account	**(61)**	(62)	(73)
Effect of exchange rate fluctuations on cash	**6**	6	5
Net increase (decrease) in Cash	**11**	(9)	(17)
Cash, beginning of year	**378**	387	404
Cash, end of year	**$ 389**	$ 378	$ 387

INTERMEDIATE FINANCING FACILITY ACCOUNT
INTER-AMERICAN DEVELOPMENT BANK

BALANCE SHEET

Expressed in millions of United States dollars

	December 31,			
	2006		2005	
ASSETS				
Cash and investments				
Cash	$ —		$ 5	
Investments	339	$339	298	$303
Accrued interest on investments		—		1
Total assets		$339		$304
FUND BALANCE				
Fund balance		$339		$304

STATEMENT OF CHANGES IN FUND BALANCE

Expressed in millions of United States dollars

	Years ended December 31,		
	2006	2005	2004
Additions			
Allocations from Fund for Special Operations	$ 61	$ 62	$ 73
Income from investments	17	9	4
Total additions	78	71	77
Deductions			
Interest and principal paid on behalf of Ordinary Capital borrowers	43	43	58
Change in fund balance, before translation adjustments	35	28	19
Translation adjustments	—	(1)	—
Change in fund balance, after translation adjustments	35	27	19
Fund balance, beginning of year	304	277	258
Fund balance, end of year	$339	$304	$277

STATEMENT OF CASH FLOWS

Expressed in millions of United States dollars

	Years ended December 31,		
	2006	2005	2004
Cash flows from operating activities			
Allocations from Fund for Special Operations	$ 61	$ 62	$ 73
Income from investments	5	9	14
Interest and principal paid on behalf of Ordinary Capital borrowers	(43)	(43)	(59)
Net increase in investments	(28)	(26)	(29)
Net cash (used in) provided by operating activities	(5)	2	(1)
Effect of exchange rate fluctuations on cash	—	—	(1)
Net (decrease) increase in Cash	(5)	2	(2)
Cash, beginning of year	5	3	5
Cash, end of year	$ —	$ 5	$ 3

TABLE XI • TEN YEARS OF IDB OPERATIONS, 1997–2006

(In millions of U.S. dollars)

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
CAPITAL										
Subscriptions (End of Year)										
Ordinary Capital	87,557	94,219	100,881	100,959	100,959	100,951	100,951	100,951	100,953	100,953
Fund for Special Operations	9,572	9,643	9,646	9,559	9,480	9,584	9,735	9,802	9,671	9,725
Other Funds[1]	2,475	2,572	2,634	2,651	2,730	2,772	2,976	3,066	3,113	3,211
Total	**99,604**	**106,434**	**113,161**	**113,169**	**113,169**	**113,307**	**113,662**	**113,819**	**113,737**	**113,889**
BORROWINGS[2]										
Outstanding (End of Year)	27,331	32,511	38,784	41,394	42,186	47,471	50,821	48,886	46,433	46,396
Gross Annual Borrowings	5,569	5,761	8,865	8,139	7,097	9,340	9,109	4,710	4,937	5,419
OPERATIONS										
Loans and Guarantees Approved (Cumulative)[3]										
Ordinary Capital[4]	68,739	79,742	88,226	89,959	93,518	100,834	110,436	116,799	118,094	125,012
Fund for Special Operations	13,580	14,273	14,663	14,924	15,328	15,774	16,652	17,391	17,486	18,257
Other Funds	1,722	1,735	1,726	1,724	1,719	1,736	1,769	1,747	1,743	1,751
Total	**84,041**	**95,750**	**104,615**	**106,607**	**110,565**	**118,344**	**128,857**	**135,937**	**137,323**	**145,020**
Loans and Guarantees Approved (Annual)[5]										
Ordinary Capital[4]	5,680	9,364	9,061	4,969	7,411	4,143	6,232	5,468	6,738	5,774
Fund for Special Operations	283	686	417	297	443	406	578	552	410	605
Other Funds	85	13	8	—	—	—	—	—	—	2
Total	**6,048**	**10,063**	**9,486**	**5,266**	**7,854**	**4,549**	**6,810**	**6,020**	**7,148**	**6,381**
Loan Disbursements (Annual)[5]										
Ordinary Capital[4]	4,958	6,085	7,947	6,683	6,037	5,522	8,416	3,768	4,899	6,088
Fund for Special Operations	493	535	430	386	422	313	486	463	424	398
Other Funds	17	15	10	—	—	2	—	1	5	3
Total	**5,468**	**6,635**	**8,387**	**7,069**	**6,459**	**5,837**	**8,902**	**4,232**	**5,328**	**6,489**
Loan Repayments (Annual)[5]										
Ordinary Capital	2,244	1,946	1,988	2,312	1,926	4,106	7,279	5,199	5,224	8,615
Fund for Special Operations	285	283	289	289	268	256	296	294	301	290
Other Funds	40	29	29	15	14	13	12	9	5	3
Total	**2,569**	**2,258**	**2,306**	**2,616**	**2,208**	**4,375**	**7,587**	**5,502**	**5,530**	**8,908**
Loans Outstanding										
Ordinary Capital	27,301	32,635	38,552	41,872	44,951	47,958	50,655	49,842	48,135	45,932
Fund for Special Operations	6,734	6,827	6,955	7,025	6,637	6,763	7,216	7,041	6,873	7,115
Other Funds	209	189	164	146	133	118	104	98	94	94
Total	**34,244**	**39,651**	**45,671**	**49,043**	**51,721**	**54,839**	**57,975**	**56,981**	**55,102**	**53,141**
Nonreimbursable Technical Cooperation Approved (Annual)[6]										
Ordinary Capital	—	—	—	—	—	—	—	—	12	34
Fund for Special Operations	88	64	47	36	39	36	30	36	36	28
Other Funds	21	53	44	34	46	45	47	39	57	52
Total	**109**	**117**	**91**	**70**	**85**	**81**	**77**	**75**	**105**	**114**
Multilateral Investment Fund Operations Approved (Annual)[7]	**62**	**127**	**141**	**100**	**90**	**99**	**69**	**116**	**113**	**125**
ADMINISTRATION										
Administrative Expenses										
TOTAL – ALL BANK FUNDS	**348**	**341**	**335**	**342**	**355**	**376**	**386**	**404**	**473**	**507**

[1] Includes the Multilateral Investment Fund.
[2] Medium- and long-term borrowings at face value, before swaps.
[3] Net of cancellations. Includes exchange adjustments.
[4] Net of non-sovereign-guaranteed loan participations.
[5] Based on original amounts in U.S. dollar equivalent.
[6] Includes Social Entrepreneurship Program financing, special programs and other grants.
[7] Includes technical cooperations, loans and equity investments.

TABLE XII • ACTIVE FUNDS IN ADMINISTRATION

Country	Name	Cumulative contributions[1] (US$ millions equivalent)
Austria	Austrian Technical Cooperation Trust Fund	1.0
	IDB Disaster Assistance and Reconstruction Fund	4.1
Belgium	Belgian Trust Fund for Consultants	3.1
Canada	Canadian Technical Cooperation Program	13.2
	IDB-Canada Trade Fund	4.7
Denmark	Danish Consultants Fund	2.8
Finland	Finnish Technical Assistance Program	1.8
France	French Technical Cooperation Fund for Consultancy and Training Activities	19.5
Israel	Israeli Consultant Trust Fund (Bank of Israel)	0.7
Italy	Italian Consulting Firms and Specialized Institutions Fund	15.8
	Italian Individual Consultant Trust Fund	7.2
	Italian Trust Fund for MIF Project Preparation	3.2
	Italian Trust Fund for Microenterprise Development	8.8
	Italian Information and Communication Technology Fund	7.0
	Italian Fund for Cultural Heritage and Sustainable Development	2.1
Japan	Japan Special Fund	221.7
	IDB Graduate Scholarship Program	31.8
	Japanese Trust Fund for Consulting Services	37.7
Korea, Republic of	Korean Trust Fund	1.0
	Korean Trust Fund for the Republic of Colombia	1.0
	Knowledge Partnership Korea Fund for Technology and Innovation	19.5
	Korea Poverty Reduction Fund	19.5
Netherlands	Partnership Program in Environment	7.0
	Netherlands Water Management Partnership Program	8.1
Norway	Norwegian Development Fund for Latin America	2.0
	Norwegian Fund for Microenterprise Development	1.9
	Norwegian Consulting Services Trust Fund	1.0
Norway and Canada	Social Capital, Ethics and Development Fund	1.8
	Gender Mainstreaming Trust Fund	3.5
Norway, United Kingdom and Canada	Social Inclusion Fund	4.8
Portugal	Portuguese Technical Cooperation Fund	1.6
Spain	Spanish Fund for Consultants (ICEX)	13.8
	Spanish Framework–General Cooperation Fund	44.4
Sweden	Swedish Framework–Sida-IDB Partnership Program	4.8
	Swedish Trust Fund for Consulting Services and Training Activities	3.1
Switzerland	Swiss Consultants Fund	5.2
United Kingdom	IDB-DFID *Enlace* Trust Fund	1.6
	Markets and Governance for Poverty Reduction Trust Fund	3.2
	Trade and Poverty Trust Fund	0.8
United States	USTDA-IDB Evergreen Fund for Technical Assistance	6.6
	Social Progress Trust Fund	525.0
Regional	Indigenous Peoples' Fund	16.1
	Regional Fund for Agricultural Technology (FONTAGRO)	36.1
World Bank	IDB/Global Environment Facility	18.8

[1] Amounts reflect historical exchange rates and do not reflect balance currently available.

TABLE XIII • DISBURSEMENTS FOR PURCHASE OF GOODS AND SERVICES BY COUNTRY OF ORIGIN (POLICY-BASED LOANS)[1]

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

	2006				1990–2006					
	Exports[2]		Total		Local Purchases		Exports		Total	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
Borrowing Countries										
Argentina	$ 54.6	3.0	$ 54.6	3.0	$ 30.0	40.2	$ 1,240.4	4.2	$ 1,270.4	4.3
Bahamas	0.0	0.0	0.0	0.0			6.4	0.0	6.4	0.0
Barbados	0.1	0.0	0.1	0.0			6.5	0.0	6.5	0.0
Belize	0.0	0.0	0.0	0.0			29.9	0.1	29.9	0.1
Bolivia	16.9	0.9	16.9	0.9			137.3	0.5	137.3	0.5
Brazil	339.6	18.6	339.6	18.6			3,783.2	12.7	3,783.2	12.7
Chile	59.2	3.2	59.2	3.2			641.9	2.2	641.9	2.2
Colombia	50.3	2.8	50.3	2.8			423.0	1.4	423.0	1.4
Costa Rica	10.5	0.6	10.5	0.6			130.2	0.4	130.2	0.4
Dominican Republic	0.0	0.0	0.0	0.0			0.6	0.0	0.6	0.0
Ecuador	52.8	2.9	52.8	2.9			461.8	1.6	461.8	1.6
El Salvador	0.0	0.0	0.0	0.0			54.8	0.2	54.8	0.2
Guatemala	9.2	0.5	9.2	0.5			81.0	0.3	81.0	0.3
Guyana	0.1	0.0	0.1	0.0			2.6	0.0	2.6	0.0
Haiti	0.0	0.0	0.0	0.0	14.6	19.5	0.0	0.0	14.6	0.1
Honduras	2.4	0.1	2.4	0.1			17.2	0.1	17.2	0.1
Jamaica	0.0	0.0	0.0	0.0			3.7	0.0	3.7	0.0
Mexico	110.3	6.0	110.3	6.0			935.7	3.1	935.7	3.1
Nicaragua	1.5	0.1	1.5	0.1	0.4	0.5	8.1	0.0	8.5	0.0
Panama	1.3	0.1	1.3	0.1	29.7	39.8	70.9	0.2	100.6	0.3
Paraguay	0.0	0.0	0.0	0.0			145.2	0.5	145.2	0.5
Peru	20.4	1.1	20.4	1.1			164.2	0.6	164.2	0.6
Suriname	0.0	0.0	0.0	0.0			1.0	0.0	1.0	0.0
Trinidad and Tobago	10.8	0.6	10.8	0.6			86.6	0.3	86.6	0.3
Uruguay	8.1	0.4	8.1	0.4			249.8	0.8	249.8	0.8
Venezuela	47.8	2.6	47.8	2.6			1,008.1	3.4	1,008.1	3.4
Total Borrowers	**$ 795.9**	**43.6**	**$ 795.9**	**43.6**	**$74.7**	**100.0**	**$ 9,690.1**	**32.6**	**$ 9,764.8**	**32.8**
Nonborrowing Countries										
Austria	$ 5.1	0.3	$ 5.1	0.3			$ 81.3	0.3	$ 81.3	0.3
Belgium	15.6	0.9	15.6	0.9			210.9	0.7	210.9	0.7
Canada	29.7	1.6	29.7	1.6			508.7	1.7	508.7	1.7
Croatia	0.2	0.0	0.2	0.0			2.8	0.0	2.8	0.0
Denmark	4.7	0.3	4.7	0.3			82.8	0.3	82.8	0.3
Finland	11.1	0.6	11.1	0.6			108.1	0.4	108.1	0.4
France	38.9	2.1	38.9	2.1			918.5	3.1	918.5	3.1
Germany	79.9	4.4	79.9	4.4			1,851.9	6.2	1,851.9	6.2
Israel	6.8	0.4	6.8	0.4			84.1	0.3	84.1	0.3
Italy	44.2	2.4	44.2	2.4			1,092.1	3.7	1,092.1	3.7
Japan	95.6	5.2	95.6	5.2			1,362.7	4.6	1,362.7	4.6
Korea, Republic of	59.7	3.3	59.7	3.3			92.1	0.3	32.4	0.1
Netherlands	27.6	1.5	27.6	1.5			515.5	1.7	515.5	1.7
Norway	2.7	0.1	2.7	0.1			51.2	0.2	51.2	0.2
Portugal	1.5	0.1	1.5	0.1			29.1	0.1	29.1	0.1
Slovenia	0.3	0.0	0.3	0.0			7.8	0.0	7.8	0.0
Spain	42.9	2.3	42.9	2.3			888.2	3.0	888.2	3.0 S
Sweden	12.4	0.7	12.4	0.7			273.0	0.9	273.0	0.9
Switzerland	18.2	1.0	18.2	1.0			376.4	1.3	376.4	1.3
United Kingdom	22.4	1.2	22.4	1.2			565.0	1.9	565.0	1.9
United States	511.9	28.0	511.9	28.0			10,961.7	36.8	10,961.7	36.8
Yugoslavia[3]	0	0.0	0.0	0.0			0.8	0.0	0.8	0.0
Total Nonborrowers	**$1,031.4**	**56.4**	**$1,031.4**	**56.4**	**0.0**	**0.0**	**$20,064.7**	**67.4**	**$20,005.0**	**67.2**
TOTAL	**$1,827.3**	**100.0**	**$1,827.3**	**100.0**	**$74.7**	**100.0**	**$29,754.8**	**100.0**	**$29,769.8**	**100.0**

[1] Policy-based lending began in 1990.
[2] Since 1998, the information in this table has reflected adjusted loan disbursements to each borrower as pro rata shares of that borrower's eligible imports from supplying countries, using the latest available import data drawn from United Nations trade statistics.
[3] In 1993, the Socialist Federal Republic of Yugoslavia ceased to be a member of the Bank.

TABLE XIV • DISBURSEMENTS FOR PURCHASE OF GOODS AND SERVICES BY COUNTRY OF ORIGIN (INVESTMENT LOANS)

(In millions of U.S. dollars)

	2006						1961–2006					
	Local Purchases		Exports[1]		Total		Local Purchases		Exports		Total	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
Borrowing Countries												
Argentina	$ 481.1	12.6	$ 18.0	7.2	$ 499.1	12.3	$ 5,073.8	10.0	$ 929.6	4.1	$ 6,003.4	8.1
Bahamas	6.6	0.2	0.0	0.0	6.6	0.2	52.4	0.1	84.8	0.4	137.2	0.2
Barbados	7.0	0.2	0.0	0.0	7.0	0.2	111.5	0.2	2.2	0.0	113.7	0.2
Belize	1.1	0.0	0.0	0.0	1.1	0.0	62.1	0.1	0.2	0.0	62.3	0.1
Bolivia	51.0	1.3	1.0	0.4	52.0	1.3	1,117.3	2.2	97.8	0.4	1,215.1	1.7
Brazil	1,348.8	35.4	21.9	8.8	1,370.7	33.7	15,349.4	30.1	2,095.6	9.2	17,445.0	23.6
Chile	64.1	1.7	3.6	1.4	67.7	1.7	2,675.8	5.3	114.4	0.5	2,790.2	3.8
Colombia	307.9	8.1	3.9	1.6	311.8	7.7	2,789.8	5.5	198.7	0.9	2,988.5	4.1
Costa Rica	22.0	0.6	1.9	0.8	23.9	0.6	459.8	0.9	191.9	0.8	651.7	0.9
Dominican Republic	50.1	1.3	0.2	0.1	50.3	1.2	691.7	1.4	37.2	0.2	728.9	1.0
Ecuador	69.6	1.8	0.2	0.1	69.8	1.7	1,858.9	3.7	59.9	0.3	1,918.8	2.6
El Salvador	62.6	1.6	3.7	1.5	66.3	1.6	996.4	2.0	51.3	0.2	1,047.7	1.4
Guatemala	63.0	1.7	1.3	0.5	64.3	1.6	758.1	1.5	83.8	0.4	841.9	1.1
Guyana	23.2	0.6	0.0	0.0	23.2	0.6	166.1	0.3	0.7	0.0	166.8	0.2
Haiti	54.8	1.4	0.0	0.0	54.8	1.4	322.5	0.6	9.6	0.0	332.1	0.5
Honduras	25.2	0.7	1.3	0.5	26.5	0.7	723.9	1.4	40.5	0.2	764.4	1.0
Jamaica	13.6	0.4	0.7	0.3	14.3	0.4	296.9	0.6	90.1	0.4	387.0	0.5
Mexico	629.0	16.5	4.4	1.8	633.4	15.6	9,458.5	18.6	765.9	3.4	10,224.4	13.9
Nicaragua	76.2	2.0	0.5	0.2	76.7	1.9	719.0	1.4	25.0	0.1	744.0	1.0
Panama	61.4	1.6	1.1	0.4	62.5	1.5	774.9	1.5	48.6	0.2	823.5	1.1
Paraguay	78.4	2.1	0.0	0.0	78.4	1.9	940.8	1.9	48.0	0.2	988.8	1.3
Peru	158.2	4.2	0.7	0.3	158.9	3.9	2,199.1	4.3	176.3	0.8	2,375.4	3.2
Suriname	7.4	0.2	0.0	0.0	7.4	0.2	16.5	0.0	1.0	0.0	17.5	0.0
Trinidad and Tobago	16.8	0.4	8.3	3.3	25.1	0.6	380.6	0.8	83.0	0.4	463.6	0.6
Uruguay	55.4	1.5	0.5	0.2	55.9	1.4	1,276.0	2.5	48.3	0.2	1,324.3	1.8
Venezuela	79.5	2.1	0.2	0.1	79.7	2.0	1,694.6	3.3	216.4	1.0	1,911.0	2.6
Total Borrowers	**$3,814.0**	**100.0**	**$ 73.4**	**29.4**	**$3,887.4**	**95.7**	**$50,966.4**	**100.0**	**$ 5,500.8**	**24.1**	**$ 56,467.2**	**76.5**
Nonborrowing Countries												
Austria			$ 1.3	0.5	$ 1.3	0.0			$ 76.7	0.3	$ 76.7	0.1
Belgium			0.1	0.0	0.1	0.0			97.0	0.4	97.0	0.1
Canada			4.9	2.0	4.9	0.1			382.2	1.7	382.2	0.5
Croatia			0.0	0.0	–	0.0			2.4	0.0	2.4	0.0
Denmark			2.8	1.1	2.8	0.1			106.9	0.5	106.9	0.1
Finland			0.0	0.0	–	0.0			50.7	0.2	50.7	0.1
France			5.9	2.4	5.9	0.2			1,376.5	6.0	1,376.5	1.9
Germany			5.1	2.0	5.1	0.1			1,420.5	6.2	1,420.5	1.9
Israel			0.3	0.1	0.3	0.0			132.8	0.6	132.8	0.2
Italy			2.8	1.1	2.8	0.1			2,059.7	9.0	2,059.7	2.8
Japan			2.7	1.1	2.7	0.1			1,246.1	5.5	1,246.1	1.7
Korea, Republic of			0.2	0.1	0.2	0.0			0.3	0.0	0.3	0.0
Netherlands			0.6	0.2	0.6	0.0			199.4	0.9	199.4	0.3
Norway			0.0	0.0	–	0.0			15.0	0.1	15.0	0.0
Portugal			0.0	0.0	–	0.0			52.8	0.2	52.8	0.1
Slovenia			0.0	0.0	–	0.0			38.2	0.2	38.2	0.1
Spain			36.5	14.6	36.5	0.9			927.9	4.1	927.9	1.3
Sweden			1.0	0.4	1.0	0.0			380.7	1.7	380.7	0.5
Switzerland			6.1	2.4	6.1	0.2			539.2	2.4	539.2	0.7
United Kingdom			4.9	2.0	4.9	0.1			649.5	2.8	649.5	0.9
United States			101.2	40.5	101.2	2.5			7,603.2	33.2	7,603.2	10.3
Yugoslavia[2]			0.0	0.0	–	0.0			13.5	0.1	13.5	0.0
Total Nonborrowers		**0.0**	**$ 176.4**	**70.6**	**$ 176.4**	**4.3**			**$ 17,371.2**	**76.0**	**$ 17,371.2**	**23.5**
TOTAL	**$3,814.0**	**100.0**	**$249.8**	**100.0**	**$4,063.8**	**100.0**	**$50,966.4**	**100.0**	**$22,872.0**	**100.0**	**$73,838.4**	**100.0**

[1] Since 1998, the information in this table has reflected adjusted loan disbursements to each borrower as pro rata shares of that borrower's eligible imports from supplying countries, using the latest available import data drawn from United Nations trade statistics.

[2] In 1993, the Socialist Federal Republic of Yugoslavia ceased to be a member of the Bank.

TABLE XV • CONSOLIDATED ADMINISTRATIVE EXPENSES

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

Category	2004 Actual	2005 Actual	2006 Actual
Board of Governors	$ 2,469.9	$ 3,797.5	$ 3,926.6
Board of Executive Directors	16,332.3	17,630.2	18,036.8
Office of Evaluation and Oversight	5,694.8	6,572.3	6,648.3
Headquarters and Country Offices	382,704.4	406,722.1	429,905.0
Total Gross Administrative Expenses[1,2,3,4,5]	**407,201.4**	**434,722.0**	**458,516.6**
Reimbursement from Funds in Administration and IIC	(2,678.1)	(3,776.3)	(3,822.8)
MIF and INTAL Reimbursements, Administrative Income	(9,844.4)	(9,479.2)	(8,656.0)
Total Net Administrative Expenses	**394,678.9**	**421,466.6**	**446,037.8**
Capital Expenses	35,521.6	23,904.1	18,590.2
Total Net Administrative and Capital Expenses	**$430,200.5**	**$445,370.7**	**$464,628.0**

[1] Excludes depreciation amounting to $11.1 million in 2004, $15.7 million in 2005 and $43.1 million in 2006.

[2] Excludes accrued pension benefit costs amounting to $7.7 million in 2005 and $4.0 million in 2006. In 2004, includes prepaid pension benefit costs amounting to $9.8 million.

[3] Excludes $14.8 million and $1.1 million of expenses in 2005 and 2006, respectively, related to prior years.

[4] Excludes amounts of $0.5 million for 2005 and $0.5 million for 2006, for the Inter-American Culture and Development Foundation.

[5] Starting in 2006, the Administrative Budget is based on Gross Amounts while all Income and Reimbursements of the Bank are recorded to income accounts. The Annual Budget Resolution is presented and approved in Gross terms by the Board of Executive Directors. Amounts reported for 2004 and 2005 actuals have been adjusted from net to gross, to reflect this change.

Management's Discussion and Analysis and Financial Statements

FINANCIAL OVERVIEW

Unless otherwise indicated, all information provided in this Management's Discussion and Analysis refers to the Bank's Ordinary Capital.

The purpose of the Bank is to further the economic and social development of Latin America and the Caribbean by promoting sustainable growth, as well as poverty reduction and social equity. The Bank is an international institution established in 1959, pursuant to the Agreement Establishing the Inter-American Development Bank (the Agreement), and is owned by its member countries. These members include 26 borrowing member countries and 21 non-borrowing member countries. The five largest members by shareholdings are the United States, Argentina, Brazil, Mexico and Venezuela.

The resources of the Bank consist of the Ordinary Capital, the Fund for Special Operations (FSO) and the Intermediate Financing Facility Account (IFF).

The financial strength of the Bank is based on the support it receives from its members and on its financial policies and practices. Member support is reflected in the capital backing received and in the diligence with which borrowing members meet their debt-service obligations. Prudent financial policies and practices have led the Bank to build its retained earnings, diversify its funding sources, hold a large portfolio of liquid investments and limit a variety of risks, including credit, market and liquidity risks. The objective of the Bank is to earn an adequate level of income to preserve its financial strength and sustain its development activities. **Box 1** presents selected financial data for the last five years.

The principal assets are loans to member countries. Up to 10% of outstanding loans and guarantees, not including emergency loans, may be made directly to private sector or (as of August 2006) sub-sovereign entities ("eligible entities") without a sovereign guarantee ("non-sovereign-guaranteed operations"), subject to certain prudential limits. As of December 31, 2006, over 97% of loans outstanding were sovereign-guaranteed.

The Bank issues debt securities in a variety of currencies, maturities, structures, and formats to investors worldwide. These borrowings, together with the Bank's equity, are used to fund lending and investment activities, as well as general operations.

Assets and liabilities are held primarily in United States dollars, euro, Japanese yen and Swiss francs. The Bank minimizes exchange rate risk by matching the currencies of its liabilities with those of its assets. The reported levels of assets, liabilities, income and expense are affected by exchange rate movements between such major currencies and the reporting currency, the United States dollar. The Bank matches the currencies of its equity with those of its loans; thus fluctuations in exchange rates do not significantly impact its risk-bearing capacity.

Financial Highlights

During 2006, the Bank approved 90 loans amounting to $5.4 billion as compared to 72 loans that totaled $6.4 billion in 2005. The decrease in the amount of loan approvals was mostly due to a decrease in investment lending that was partially offset by an increase in policy-based and non-sovereign-guaranteed lending. Also, disbursements in 2006 totaled the equivalent of $6.1 billion, higher than the $4.9 billion disbursed in 2005. The undisbursed portion of approved loans decreased to $16.1 billion at year-end 2006 from $17.0 billion at year-end 2005.

As of December 31, 2006, all loans were performing, except for certain loans to some private sector borrowers without sovereign guarantee in the aggregate amount of $66 million (2005—$196 million). The allowances for loan and guarantee losses amounted to $104 million compared to $188 million in 2005. The decrease was mainly due to a reduction in the allowance for private sector impaired loans resulting from better than expected loan collections, as well as loan write offs of $42 million.

In April 2006, the Board of Governors authorized the Board of Executive Directors to expand the scope of authority regarding private sector financing without sovereign guarantees under the 10% limit (a) to encompass projects in all sectors, subject to an exclusion list, thereby eliminating restrictions previously limiting such financing only to infrastructure, capital markets and trade finance operations and (b) to include sub-sovereigns. In August 2006, the Board of Executive Directors approved an integrated business plan and revised operational guidelines for operations without sovereign guarantees, making this authorization effective.

In 2006, the Bank issued medium- and long-term debt securities for a total face amount of $5.4 billion equivalent (2005—$4.9 billion), that generated proceeds of $5.3 billion equivalent (2005—$4.9 billion) and had an average life of 6.5 years (2005—6.3 years). Such debt securities were issued through a strategy of combining large global benchmark bonds with smaller transactions targeted to particular segments of demand. The increase in 2006 borrowings was primarily attributable to greater flexibility in the Bank's capital markets operations resulting from the new liquidity policy approved in 2005.

The Bank enters into currency and interest rate swaps to manage its interest and exchange rate exposures as part of its borrowing operations. According to SFAS 133, these derivatives are valued at their fair value with changes in fair value recorded in income. Management believes that the reported income volatility of applying SFAS 133 is not representative of the underlying economics of the transactions as the Bank generally holds its derivatives and related bonds to maturity. Accordingly, Income before SFAS 133 and currency transaction adjustments[1] is defined herein as "Operating Income", which is more representative of the net results of the Bank's operations. The effects of SFAS 133 and currency transaction adjustments are shown separately in the Statement of Income and Retained Earnings and are excluded from the determination of ratios and other financial parameters.

[1]References to captions in the financial statements and related notes are identified by the name of the caption beginning with a capital letter every time they appear in this Management's Discussion and Analysis.

Operating Income was $627 million in 2006 compared with $712 million in 2005. The decrease was largely due to a reduction in net interest income generated by the loan portfolio (primarily due to a reduction in loan charges and a decrease in outstanding emergency loans, partially offset by an increase in the income generated by the Bank's equity resources) and an increase in net non-interest expenses, partially offset by a higher credit for loan and guarantee losses. Against a background of steady growth in the Total Equity to Loans Ratio or TELR[2] in recent years, which surpassed the desired level of 38% during 2006, the Board of Executive Directors approved lower than standard loan charges for sovereign-guaranteed, non-emergency loans of 0.10% and 0.15% lending spread for the first and second semester, respectively, 0.10% credit commission and no supervision and inspection fee. Changes in market interest rates generally do not significantly affect Operating Income, as a substantial amount of the loans are cost pass-through loans, and the Bank matches the interest rate structures of its liquid assets and the liabilities funding them.

[2]The TELR is the ratio of the sum of "equity" (defined as Paid-in capital stock, Retained earnings and the allowances for loan and guarantee losses, minus borrowing countries' local currency cash balances, net receivable from members, Postretirement benefit assets and the cumulative impact of SFAS 133 and currency transaction adjustments) to outstanding loans and net guarantee exposure.

The Effects of SFAS 133 and currency transaction adjustments for 2006 was higher than in the previous year ($384 million negative versus $50 million positive) mostly due to the increase in long-term interest rates during the year. During 2006, the impact of interest rates on the value of borrowing and lending swaps amounted to a decrease in income of $469 million, compared to an increase of $5 million in 2005.

The Bank manages its financial condition by monitoring certain financial ratios, in particular the TELR. The TELR at December 31, 2006, was 40.8% compared with 37.3% at December 31, 2005, with the increase mainly due to the combination of an increase in equity resulting from operating income and a decline in loans outstanding, mostly from prepayments of $4.3 billion. According to the Bank's capital adequacy policy, as long as Operating Income is positive and the TELR is within a range between 32% and 38% and increasing over the medium term, the Bank will apply standard loan charges, equal to a lending spread of 0.30%, a credit commission of 0.25%, and no supervision and inspection fee. Management has presented to the Board of Executive Directors a consultation document on options for the use of equity exceeding 38%. The Board of Executive Directors has the matter under consultation.

The above information is qualified by the detailed information and financial statements appearing elsewhere in this section. In addition, the Management's Discussion and Analysis contains forward-looking information, which may be identified by such terms as "believes", "expects", "intends" or words of similar meaning. Such statements involve a number of assumptions and estimates that are based on current expectations, which are subject to risks and uncertainties beyond the Bank's control. Consequently, actual future results could differ materially from those currently anticipated. The Bank undertakes no obligation to update any forward-looking statements.

Box 1: Selected Financial Data

The following information is based upon, and should be read in conjunction with, the detailed information appearing in this Management's Discussion and Analysis and the financial statements for the Ordinary Capital included in this Annual Report.

(Amounts expressed in millions of United States dollars)

	Years ended December 31,				
	2006	2005	2004	2003	2002
Balance Sheet Data					
Cash and investments-net[1], after swaps	$16,051	$13,717	$13,046	$14,855	$14,780
Approved loans					
Loans outstanding	45,932	48,135	49,842	50,655	47,958
Undisbursed portion of approved loans	16,080	17,000	16,093	15,619	18,570
Total assets	66,475	65,382	67,346	69,669	65,031
Borrowings outstanding[2], after swaps	43,550	43,988	45,144	49,275	48,179
Equity					
Callable capital stock	96,613	96,613	96,611	96,611	96,611
(of which, subscribed by United States, Japan, Canada and the other nonregional members)	48,302	48,302	48,300	48,300	48,300
Paid-in capital stock	4,340	4,340	4,340	4,340	4,340
Retained earnings[3]	15,468	14,387	14,171	12,772	9,929
Total equity	19,808	18,727	18,511	17,112	14,269
Income Statement Data					
Loan income	$ 2,466	$ 2,413	$ 2,498	$ 2,711	$ 2,639
Investment income	619	403	288	298	319
Borrowing expenses, after swaps	2,070	1,733	1,572	1,636	1,842
Loan and guarantee loss provision (credit)[4]	(48)	(14)	21	(1,370)	100
Net non-interest expense	436	385	331	309	289
Operating Income	627	712	862	2,434	727
Effects of SFAS 133 and currency transaction adjustments[5][6]	(384)	50	314	(1)	(19)
Net income.	243	762	1,176	2,433	708
Ratios					
Net borrowings[7] as a percentage of callable capital stock subscribed by United States, Japan, Canada and the other nonregional members	57.9%	63.5%	67.3%	72.1%	70.0%
Interest coverage ratio[4]	1.30	1.41	1.55	2.49	1.40
Total equity[8] to loans[9] ratio (TELR)	40.8%	37.3%	36.1%	33.0%	30.9%
Cash and investments as a percentage of borrowings outstanding, after swaps	36.9%	31.2%	28.9%	30.1%	30.7%
Returns and Costs, after swaps					
Return on:					
Average loans outstanding	5.22%	5.04%	5.02%	5.51%	5.73%
Average liquid investments	4.39%	3.29%	2.17%	2.00%	2.28%
Average earning assets	5.02%	4.68%	4.42%	4.70%	4.91%
Average cost of:					
Borrowings outstanding during the year	4.78%	4.07%	3.40%	3.37%	3.97%
Total funds available	3.40%	2.92%	2.53%	2.57%	3.09%
Term Duration (in years)					
Investments and loans	4.49	4.41	4.36	4.33	4.13
Debt	3.89	4.00	4.15	4.46	3.66

(1) Net of Payable for investment securities purchased.
(2) Net of premium/discount.
(3) Includes Accumulated other comprehensive income.
(4) The interest coverage ratio is computed using Operating Income and, in 2003, included a one-time reduction in the Allowance for loan losses of $1.4 billion, which was credited to income.
(5) SFAS 133 refers to Statement of Financial Accounting Standards 133 "Accounting for Derivative Instruments and Hedging Activities", along with its related amendments.
(6) Effective January 1, 2004, the Bank discontinued the use of hedge accounting, resulting in a higher impact of SFAS 133.
(7) Borrowings (after swaps) and gross guarantee exposure, less qualified liquid assets (after swaps) and the special reserve assets.
(8) Paid-in capital stock, Retained earnings and the allowances for loan and guarantee losses, minus borrowing countries' local currency cash balances, net receivable from members, Postretirement benefit assets and the cumulative effects of SFAS 133 and currency transaction adjustments.
(9) Includes loans outstanding and net guarantee exposure.

DEVELOPMENT OPERATIONS

General

The Bank offers loans and guarantees to the governments, as well as governmental entities, enterprises, and development institutions of its borrowing member countries to help meet their development needs. Loans and guarantees may also be made directly to private sector entities carrying out projects in the territories of borrowing member countries without a sovereign guarantee, provided they meet the Bank's lending criteria. In addition, effective August 2006, the Bank expanded the scope of authority for lending to private sector entities to include sub-sovereign entities without the support of sovereign guarantees, as well as financings in all sectors. The Bank also provides financing to borrowing member countries for non-reimbursable and contingent recovery assistance that is aligned with its overall strategy for the region.

Development Objectives

The Bank's two main goals are to promote sustainable growth, as well as poverty reduction and social equity. To attain these goals, the Bank focuses its work on four priority areas:

- Fostering competitiveness through support for policies and programs that increase a country's potential for development in an open global economy.
- Modernizing the state by strengthening the efficiency and transparency of public institutions.
- Investing in social programs that expand opportunities for the poor.
- Promoting regional economic integration by forging links among countries to develop larger markets for their goods and services.

Lending Cycle

The process of identifying and assessing a project and approving and disbursing a loan often extends over several years. However, on numerous occasions the Bank has shortened the preparation and approval cycle in response to emergency situations such as natural disasters or economic crises. Generally, the Bank's operational staff (economists, engineers, financial analysts and other sector and country specialists) assess the projects. With certain exceptions, the Bank's Board of Executive Directors must approve each loan.

Loan disbursements are subject to the fulfillment of conditions set out in the loan agreement. During implementation of the Bank-supported operations, experienced Bank staff review progress, monitor compliance with Bank policies and assist in resolving any problems that may arise. An independent Bank unit, the Office of Evaluation and Oversight, pursuant to an annual work plan approved by the Board of Executive Directors, evaluates some operations to determine the extent to which they have met their major objectives, and these evaluations are reported directly to the Board of Executive Directors.

The Bank's lending operations conform to certain principles that, when combined, seek to ensure that loans made to member countries are for financially and economically sound purposes to which these countries have assigned high priority, and that funds lent are utilized as intended. These principles are detailed in **Box 2** below.

Box 2: Lending Operations Principles

(i) The Bank makes sovereign-guaranteed loans and guarantees primarily to the public sector governments, as well as governmental entities, enterprises, and development institutions of its borrowing members. In addition, the Bank makes non-sovereign-guaranteed loans and guarantees to eligible entities.

(ii) Loan applicants must submit a detailed proposal to the Bank specifying the technical, economic and financial merits of the project. The proposal must include an evaluation of the project's expected environmental risks or impact and proposed mitigation measures as well as its impact on women and indigenous groups, as applicable.

(iii) The Bank neither renegotiates nor takes part in debt rescheduling agreements with respect to its sovereign-guaranteed loans.

(iv) Loan agreements typically include a negative pledge clause that generally prohibits a borrower from creating any encumbrances on its assets or revenues with respect to its foreign currency debt, unless the Bank is equally and proportionally secured. The Board of Executive Directors has granted limited waivers in the past.

(v) In making loans, the Bank evaluates the capacity of the borrower to carry out its financial obligations under the loan agreement, the prevailing macroeconomic climate and debt burden of the country, and policy and institutional issues relevant to the loan.

(vi) The Bank considers the ability of the borrower to obtain private financing under reasonable terms and conditions. The Bank serves as a catalyst to promote private investment, not to compete with it.

(vii) The use of loan proceeds is supervised. Bank staff monitor and supervise the on-going progress with respect to the development objectives of each operation through the Bank's Country Offices in each of its 26 borrowing member countries, and fiduciary arrangements are in place to ensure proper use of Bank resources to achieve the operation's objectives.

Loans

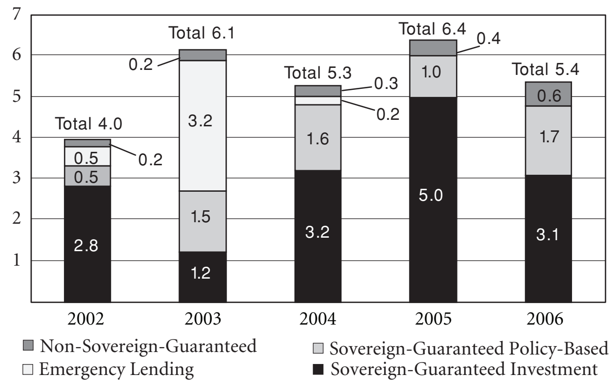
The Bank's sovereign-guaranteed lending generally falls into one of two categories: investment loans for specific projects or policy-based sector loans. Investment lending is generally used to finance goods, works and services in support of economic and social development projects in a broad range of sectors. Policy-based lending generally supports social, structural and institutional reforms with the aim of improving specific sectors of the borrowers' economies and promoting sustainable growth. These loans support the following economic sectors: energy, industry and mining, agriculture and fisheries, transportation and communications, trade finance, education, science and technology, water, sanitation and health, tourism, urban development, planning and reform, modernization of the state and the environment, as well as project preparation. The Bank has also instituted a program of emergency lending to address financial or economic crises.

In addition, the Bank lends directly to eligible entities without a sovereign guarantee for the financing of investments for transactions in all sectors, subject to an exclusion list. These loans and guarantees are made on the basis of market-based pricing, are subject to certain eligibility requirements and cannot exceed 10% of the Bank's outstanding loans and guarantees, excluding emergency lending. Such non-sovereign-guaranteed loans and guarantees are also subject to certain prudential limits, including a ceiling on financing the lesser of $200 million or 50% of the total project cost for expansion projects and credit guarantees, subject to such financing not exceeding 25% (certain countries 40%) of a company's total capitalization of debt and equity, and 25% of the total project cost (certain countries 40%) for new projects. The Bank can also provide political risk guarantees of up to the lesser of $200 million or 50% of the total project cost. In exceptional circumstances, the Board of Executive Directors may approve loans and credit and political guarantees of up to $400 million. In addition, the Bank's maximum exposure to any single obligor for non-sovereign-guaranteed operations cannot exceed 2.5% of the Bank's equity at the time of approval.

Figure 1 presents a breakdown of approvals by loan type during the last five years. Over the past five years, sovereign-guaranteed investment lending per year has fluctuated between $1.2 billion and $5.0 billion, and policy-based lending between $0.5 billion and $1.7 billion. Approvals under the Emergency Lending Facility amounted to $0.5 billion, $3.2 billion and $0.2 billion in 2002, 2003, and 2004, respectively, with no approvals in 2005 and 2006.

Under the New Lending Framework for 2005 to 2008, the Bank has more flexibility in lending up to a maximum cumulative amount of $20.6 billion for investment loans and $9.8 billion for policy-based loans and a $6 billion limit for outstanding emergency loans. Under this Lending Framework there are no minimum disbursement periods for investment and policy-based loans and policy-based loans can be made with single-tranche disbursements.

Figure 1: LOAN APPROVALS BY TYPE
For the years ended December 31, 2002 through 2006
(Expressed in billions of United States dollars)



During 2006, loan approvals totaled $5.4 billion (2005—$6.4 billion). A summary of loan approvals by country during 2006 and 2005 appears in **Table 1**. Loan approvals decreased during 2006 as a result of a reduction of $1.9 billion in the amount of investment loans approved, partially offset by increases of $0.7 billion and $0.2 billion in policy-based and non-sovereign-guaranteed loans, respectively.

Table 1: LOAN APPROVALS BY COUNTRY[(1)]
For the years ended December 31, 2006 and 2005
(Expressed in millions of United States dollars)

COUNTRY	2006	2005
Argentina	$1,626	$1,033
Bahamas	9	35
Barbados	1	4
Belize	25	—
Brazil	479	547
Chile	213	41
Colombia	580	561
Costa Rica	70	132
Dominican Republic	181	25
Ecuador	315	88
El Salvador	100	211
Guatemala	239	19
Mexico	207	2,050
Panama	304	35
Paraguay	252	45
Peru	475	345
Suriname	—	4
Trinidad and Tobago	28	2
Uruguay	191	268
Venezuela	26	910
Regional	60	85
Total	$5,381	$6,440

(1) Includes non-sovereign-guaranteed loans.

At December 31, 2006, the total volume of outstanding loans was $45.9 billion, $2.2 billion lower than the $48.1 billion at December 31, 2005. This decrease was mainly due to a higher level of loan collections ($8.6 billion, including prepayments of

$4.3 billion) than disbursements ($6.1 billion), partially offset by positive currency translation adjustments of $0.4 billion. Undisbursed balances at December 31, 2006, totaled $16.1 billion, a decrease of $0.9 billion from December 31, 2005. This change was mainly due to disbursements and cancellations, partially offset by new approvals.

Under the Agreement, the total amount of outstanding loans and guarantees may not exceed, at any time, the total amount of subscribed capital, plus reserves and surplus, exclusive of income assigned to certain reserves, including a special reserve to meet borrowings and guarantee obligations. The Bank's policy, however, is more stringent and limits the total amount of outstanding loans and guarantees to its paid-in capital stock plus the general reserve and the callable capital stock of non-borrowing member countries. At December 31, 2006, the total amount of loans outstanding and gross guarantee exposure as a percentage of the policy limit of $65.6 billion, after excluding the cumulative effects of SFAS 133 and currency transaction adjustments, was 70.5% compared to 75.4% in 2005.

A summary statement of loans outstanding by country at December 31, 2006 and 2005 is set forth in Appendix I-3 to the financial statements.

Financial Terms of Loans

Currently Available Financial Terms

The Bank currently offers a product mix that provides borrowers with flexibility to select terms that are compatible with their debt management strategy. **Table 2** presents the currently available financial terms for sovereign-guaranteed loans. As of December 31, 2006, the Bank offers two basic types of loans, each denominated in the currency or currencies chosen by the borrower, as available under the programs: Single Currency Facility (SCF) adjustable rate and SCF LIBOR-based loans. SCF adjustable rate loans, introduced in 1996, have an interest rate that is adjusted every six months to reflect the currency-specific effective cost of the pool of borrowings allocated to such loans, plus the Bank's spread. The SCF LIBOR-based loans, introduced in 2003, have an interest rate that is adjusted quarterly, based on the currency-specific three-month LIBOR plus a pool-based margin reflecting the Bank's sub-LIBOR funding cost and the risk mitigation costs, as well as the Bank's spread.

The Bank also offers U.S. Dollar Window Program loans (currently limited to $500 million of loan approvals per calendar year) destined for on-lending to private sector borrowers, as well as emergency loans, with sovereign guarantee. In addition, the Bank offers loans to eligible entities without sovereign guarantees, under various terms. Non-sovereign-guaranteed loans are denominated in United States dollars and borrowers have the option of either LIBOR-based fixed interest rate loans or floating rate loans. For fixed rate loans, the interest rate is fixed upon signature or for each disbursement, at a rate based on a LIBOR funding cost plus the lending spread. For floating rate loans, the interest rate resets every one, three or six months based on a LIBOR rate plus the lending spread. Lending spreads and fees are set on a case-by-case basis.

Under the Local Currency Facility (LCF) approved in 2005, public and private sector borrowers have the option to receive local currency financing under three different modalities: i) local currency conversion of future loan disbursements and/or outstanding loan balances; ii) direct swaps into local currency against existing Bank debt; and iii) local currency con-

Table 2: CURRENTLY AVAILABLE FINANCIAL TERMS OF LOANS WITH SOVEREIGN GUARANTEE[3]

	Single Currency Facility		U.S. Dollar Window		Emergency Lending
Interest rate option	**Adjustable rate loans**	**LIBOR-based loans**	**Fixed rate loans**	**LIBOR-based loans**	**LIBOR-based loans**
Currencies offered	USD, EUR, JPY, CHF or a combination of these currencies		USD		USD
Cost base	Weighted average cost of allocated debt	3-month LIBOR	LIBOR-based funding cost	6-month LIBOR	6-month LIBOR
Funding cost margin		Weighted average cost margin of debt allocated to this product		Weighted average cost margin of debt allocated to this product	
Risk mitigation cost[1]	Not applicable	50	Not applicable	Not applicable	Not applicable
Lending spread[1][2]	30	30	30	30	400
Credit commission[1][2]	25	25	25	25	75
Front-end fee[1]	Not applicable	Not applicable	Not applicable	Not applicable	100
Supervision and inspection fee[1][2]	0	0	0	0	Not applicable
Maturity	15–25 years		12 years	20 years	5 years
Grace period	For investment loans: original disbursement period For policy-based loans: 5 years		5 years		3 years

[1] Loan charges provided in basis points (bps).

[2] Standard loan charges on sovereign-guaranteed, non-emergency loans are subject to semi-annual review and approval by the Board of Executive Directors. See **Table 4** for information on most recently approved loan charges.

[3] Under the LCF, borrowers have the option to convert future loan disbursements and/or outstanding loan balances to local currency under certain terms and conditions.

version of called guarantees. The use of these modalities is subject to the availability of the respective local currency and the appropriate risk mitigation instrument(s) in the financial markets. Outstanding loan balances in the LCF can carry a fixed, floating or inflation-linked interest rate. At December 31, 2006, the Bank had local currency loans outstanding of $74 million.

Previously Available Financial Terms

In previous years, the Bank offered loans under a Currency Pooling System (CPS) established in 1982 and discontinued in 2003. The Bank maintains a targeted currency composition in the CPS of 50% United States dollars, 25% Japanese yen and 25% European currencies. Loans approved prior to 1989 carry a fixed interest rate while loans approved from 1990 to 2003 carry an adjustable rate. The adjustable rate, which resets twice a year, represents the effective cost during the previous six months of a pool of borrowings allocated to fund such loans, plus the Bank's spread. At December 31, 2006, these loans represented 35.5% (2005—36.9%) of loans outstanding.

Table 3 presents a breakdown of the loan portfolio by loan product. For more information, see Appendix I-4 to the financial statements.

Table 3: LOANS OUTSTANDING BY LOAN PRODUCT
December 31, 2006 and 2005
(Amounts expressed in millions of United States dollars)

	2006		2005	
	Amount	**%**	**Amount**	**%**
Single Currency Facility-adjustable	$21,505	46.8	$23,293	48.4
Single Currency Facility-LIBOR-based	4,643	10.1	2,478	5.1
U.S. Dollar Window	714	1.5	777	1.6
Emergency Lending	1,520	3.3	2,520	5.2
Non-sovereign-guaranteed Loans	1,089	2.4	1,138	2.4
Currency Pooling System	16,299	35.5	17,753	36.9
Others	162	0.4	176	0.4
Total	$45,932	100.0	$48,135	100.0

Of the $16.1 billion undisbursed loan balances at December 31, 2006, 48% pertains to the SCF-adjustable and 39% to the SCF-LIBOR-based portfolios.

Charges on Loans with Sovereign Guarantee (Excluding Emergency Lending)

The Bank's standard loan charges for loans made under the SCF, the U.S. Dollar Window Program and the CPS consist of a lending spread of 0.30% per annum on the outstanding amount, a credit commission of 0.25% per annum on the undisbursed amount of the loan, and no supervision and inspection fee. Loan charges are subject to semi-annual approval by the Board of Executive Directors. Against a background of steady growth in recent years of the TELR, which surpassed the desired level of 38% during 2006, the Board of Executive Directors approved lower than standard loan charges. **Table 4** shows loan charges prevailing during the periods indicated.

Table 4: LOAN CHARGES

	Lending spread %	Credit commission %	Supervision and inspection fee %
2004:	0.30	0.25	—
2005:			
First semester	0.30	0.25	—
Second semester	0.10	0.10	—
2006:			
First semester	0.10	0.10	—
Second semester	0.15	0.10	—

Guarantees

The Bank may make partial political risk and partial credit guarantees either without a sovereign counter-guarantee under the 10% limit established for non-sovereign-guaranteed operations, or with a member country sovereign counter-guarantee. These guarantees are denominated in United States dollars or in local currency. Regardless of the currency in which a guarantee is denominated, the Bank's exposure is, in all cases, capped at an amount in United States dollars determined at the time each guarantee is approved.

As part of its non-sovereign-guaranteed lending activities, the Bank has issued partial political risk and partial credit guarantees designed to encourage private sector infrastructure investments, local capital market development, and trade finance. The partial political risk guarantees and partial credit guarantees may be offered on a stand-alone basis or in conjunction with a Bank loan. Partial political risk guarantees cover specific risk events related to noncommercial factors (such as currency convertibility, transferability of currencies outside the host country, and government non-performance). Partial credit guarantees cover payment risks for debt obligations or trade-finance transactions. The terms of all guarantees are specifically set in each guarantee agreement and are primarily tied to a project, the terms of debt issuances or trade-finance transactions. On a case-by-case basis, depending upon the risks covered and the nature of each individual project, the Bank may reinsure certain guarantees to reduce its exposure. Guarantee exposure is measured as the future guaranteed cash flows, net of reinsurance, when applicable, discounted to the current period.

During 2006, two non-trade-related guarantees without a sovereign counter-guarantee were approved for $180 million compared to one guarantee for $28 million in 2005. In addition, the Bank approved its first partial credit guarantee operation with sovereign counter-guarantee for $60 million. The Bank has a Trade Finance Facilitation Program to provide partial credit guarantees without sovereign counter-guarantees on trade-finance transactions. This Program, which began to operate in July 2005, authorizes up to $40 million in credit support per approved trade-finance bank, and an aggregate of no more than $400 million outstanding at any time. During 2006, ten trade-finance guarantee lines of credit in the aggregate amount of $133 million were authorized and an already existing line of credit was increased by $20 million, while 36 guarantees for a total of $68 million were issued during the year. This compares with ten lines of credit in the aggregate amount of $270 million authorized and nine guarantees for a total of $19 million issued in 2005.

As of December 31, 2006, guarantees of $379 million (2005—$319 million) were outstanding and subject to call. No guarantees have ever been called. The net present value of guarantee exposure on non-sovereign guarantees, net of reinsurance, which is the amount counted towards the non-sovereign-guaranteed operations 10% limit, was $215 million at December 31, 2006 (2005—$203 million).

LIQUIDITY MANAGEMENT

The Bank invests its liquid assets in highly rated debt securities and bank deposits. These instruments include obligations of highly rated governments, government agencies, multilateral organizations, financial institutions, and corporate entities, including asset-backed securities. In addition, the Bank uses derivatives, mostly currency and interest rate swaps, to manage its investment portfolios.

Liquidity plays a key role in the management of the Bank's funding risks by addressing the risk that the Bank may not have adequate funds to meet both future loan disbursement and debt service obligations. The objective of liquidity management is to ensure that adequate resources are available to meet anticipated contractual obligations and to ensure uninterrupted financial operations in the event the Bank were to refrain from borrowing in response to unattractive market conditions or other constraints. The Bank's liquidity management principles are set forth in **Box 3** below.

Box 3: Liquidity Management Principles

The primary objective in the management of the Bank's liquidity is to limit exposure to credit, market and liquidity risks. Within the constraints determined by this primary objective, the Bank strives to maximize returns on the invested asset portfolio while limiting the volatility of the Bank's net investment income, which is the spread between investment returns and funding costs.

The Bank manages its liquidity through financial policies, instruments and guidelines, which serve as the rules, procedures and tools that define the Bank's liquidity management. The Investment Resolution approved by the Board of Executive Directors provides the basic authority within which liquidity is invested. The Investment Guidelines approved by management establish the detailed operating, compliance and monitoring conditions for the implementation of the liquidity management. Both are designed to ensure that the Bank assesses market and credit risks, and establishes investment constraints consistent with the Bank's level of risk tolerance. For information concerning the management of risk exposures on liquidity see "Financial Risk Management" below.

Under its liquidity policy, the Bank establishes yearly minimum and maximum liquidity levels, computed at 20% and 40%, respectively, of the projected year-end outstanding loan balance, and a desired level of 30%. For 2006, the liquidity level was established to range between $9.7 billion and $19.4 billion, with the mid-point of $14.6 billion being the desired level. At December 31, 2006, the Bank's liquidity (largely comprised of net cash and investments, after swaps, minus short-term borrowings and borrowing countries' local currency cash balances) was $15.2 billion. During the year, liquidity averaged $13.6 billion compared to $11.9 billion in 2005.

The Bank has short-term borrowing facilities that consist of a discount note program and uncommitted borrowing lines from various commercial banks. Discount notes are issued in amounts of not less than $100,000, with maturities of no more than 360 days. These short-term funding facilities are used to cover short-term cash flow needs.

Liquid investments are maintained in three distinct sub-portfolios: transactional, operational and held-to-maturity (HTM), each with different risk profiles and performance benchmarks. The transactional portfolio is used to meet the day-to-day cash flow requirements. The operational portfolio holds the majority of the Bank's liquid holdings. The HTM portfolio consists primarily of the special reserve assets.

Investments of up to 10% of the portfolio may be contracted out to external managers. Separate investment guidelines that conform to the Bank's overall Investment Guidelines are provided to each external manager. At December 31, 2006, the Bank had investments of $407 million managed by external firms.

The returns of the liquid investment portfolios in 2006 and 2005 are shown in **Table 5**. The higher yield levels on the total portfolio in 2006, as compared to 2005, are primarily due to the overall increase in short-term interest rates as more than three-quarters of the investments are floating rate (LIBOR-indexed). The yield level on LIBOR-based investments does not affect net income since they are financed with matching LIBOR-indexed debt. HTM yields remained substantially unchanged during the year.

Table 5: LIQUID INVESTMENT PORTFOLIOS[1]
December 31, 2006 and 2005
(Amounts expressed in millions of United States dollars)

	2006		2005	
Portfolio	**Ending Balance**	**Financial Return (%)[2]**	**Ending Balance**	**Financial Return (%)[2]**
Transactional	$ 224	5.19	$ 267	3.32
Operational	12,013	4.72	9,851	3.28
Held-to-Maturity	3,538	3.31	3,376	3.33
Overall Portfolio	$15,775	4.39	$13,494	3.29

[1] After swaps and net of Payable for investment securities purchased.
[2] Combined return for all currencies in each portfolio.

Contractual Obligations

In the normal course of business, the Bank enters into various contractual obligations that require future cash payments. The most significant contractual obligations relate to the repayment of borrowings. The maturity structure of medium- and long-term borrowings outstanding at December 31, 2006 is presented in Appendix I-5 to the financial statements. In addition, the Bank has a number of other obligations to be settled in cash, which are reflected in its financial statements, including undisbursed loans, short-term borrowings, payable for currency and interest rate swaps, and payable for investment securities purchased.

SOURCES OF FUNDS

Equity

Total equity at December 31, 2006, was $19.8 billion compared with $18.7 billion at December 31, 2005. The increase primarily reflects the net income for the year, the recognition of the remaining overfunded status of the Bank's pension and postretirement benefit plans according to SFAS 158 of $681 million, and positive translation adjustments of $149 million.

The Bank's equity base plays a critical role in securing its financial objectives, enabling the Bank to absorb risk out of its own resources and protecting member countries from a possible call on callable capital stock. For risk management purposes, the Bank monitors equity as defined and utilized in the TELR, which measures the adequacy of its risk-bearing capacity. **Table 6** presents the composition of this measure at December 31, 2006 and 2005. See "Financial Risk Management—Credit Risk—Capital Adequacy Framework" below, for more information on the TELR.

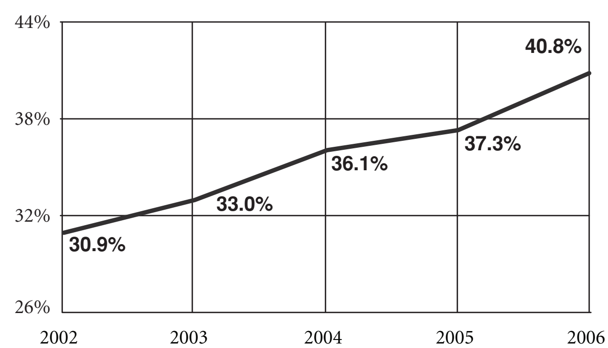
Table 6: TOTAL EQUITY TO LOANS RATIO
December 31, 2006 and 2005
(Amounts expressed in millions of United States dollars)

	2006	2005
Equity		
Paid-in capital stock	$ 4,340	$ 4,340
Retained earnings:		
General reserve[1]	12,971	11,921
Special reserve[1]	2,497	2,466
Plus:		
Allowances for loan and guarantee losses	104	188
Minus:		
Borrowing countries' local currency cash balances	142	137
Net receivable from members	103	255
Postretirement benefit assets	863	136[3]
Cumulative effects of SFAS 133 and currency transaction adjustments[2]	(27)	348
Equity used in Total Equity to Loans Ratio	$18,831	$18,039
Loans outstanding and net guarantee exposure	$46,199	$48,338
Total Equity to Loans Ratio	**40.8%**	**37.3%**

[1] Includes Accumulated other comprehensive income.
[2] Includes cumulative effect of SFAS 133 on cash flow hedges for $1 million and $8 million in 2006 and 2005, respectively.
[3] In 2005, excludes prepaid postretirement benefit costs of $51 million.

As presented in **Table 6**, the TELR increased from 37.3% at December 31, 2005, to 40.8% at December 31, 2006. The increase was mainly due to the combination of an increase in equity resulting from operating income, and a net decline of $2.2 billion in loans outstanding. The TELR has increased steadily during the last five years, as shown in **Figure 2**, reflecting a relatively higher growth rate in the equity base than in loans outstanding.

Figure 2: TOTAL EQUITY TO LOANS RATIO



Capitalization

Shareholders' support for the Bank is reflected in the capital backing it has received from its members. At December 31, 2006, subscribed capital stock was $100.9 billion, of which $4.3 billion had been paid in and $96.6 billion was callable.

Paid-in and callable capital stock subscriptions are payable as follows:

Paid-in capital stock: Each subscription to paid-in capital stock has been paid, in whole or in part, in gold, United States dollars, or the currency of the respective member country. In the case of most payments made in the currency of the respective member country, the member country has made arrangements satisfactory to the Bank to assure that, subject to the provisions of the Agreement, its currency will be freely convertible (or the member country has agreed to convert its currency on behalf of the Bank) into the currencies of other countries for the purposes of the Bank's operations. The Bank has accepted non-negotiable, non-interest-bearing demand obligations in lieu of the immediate payment of all or a part of the member's subscription to the paid-in capital stock. Under the Agreement such obligations are accepted where currencies are not required for the Bank's operations.

Callable capital stock: The callable portion of the capital stock subscriptions is subject to call only when required and to the extent necessary to meet the obligations of the Bank on borrowings of funds or guarantees. In the event of a call, payment may be made at the option of the member in gold, United States dollars, fully convertible currency of the member country or in the currency required to discharge the obligations of the Bank for the purpose for which the call is made. Calls are required to be uniform, but obligations of the members of the Bank to make payment upon such calls are independent of each other. Failure of one or more members to make payments on any such call would not excuse any other member from its obligation to make payment, and successive calls could be made on non-defaulting members if necessary to meet the Bank's obligations. However, no member could be required on any such call to pay more than the unpaid balance of its capital stock subscription. No call has ever been made on the Bank's callable capital stock.

At December 31, 2006, the total subscription of the United States, the Bank's largest shareholder, was $30.3 billion, of which the United States had paid $1.3 billion as subscriptions to the Bank's paid-in capital stock. Of the United States' callable capital stock subscription of $29.0 billion, $3.8 billion had been fully authorized and appropriated, without fiscal year limitation, by United States legislation, and no further appropriation is necessary to enable the Secretary of the Treasury to pay this amount if any part were to be called to meet obligations of the Bank. The balance of the United States' callable capital stock subscription, $25.2 billion, has been authorized by the United States Congress but not yet appropriated. In 1979, in connection with the United States' subscription to an increase in the callable capital stock, the Bank obtained an opinion of the General Counsel of the Treasury stating that appropriations were not legally required to back subscriptions to such callable capital stock unless and until payment was required of the United States on a call made by the Bank. The opinion further states that an appropriation is not required to make United States callable capital stock subscriptions, authorized by United States legislation, binding obligations backed by the full faith and credit of the United States, and that an obligation contracted by the United States pursuant to a Congressional grant of authority for constitutional purposes is fully binding on the United States notwithstanding that a future appropriation might be necessary in order to fund that obligation.

Borrowings

The Bank raises funds in the international capital markets primarily through the issuance of debt securities. To diversify its sources of funding, the Bank issues its debt securities in various currencies, maturities, formats, and structures to meet the needs of global institutional and retail investors. Under the Agreement, the Bank may borrow only with the approval of the member country in whose markets the debt securities are sold and the member country in whose currency the borrowings are denominated. In addition, the Bank is required to obtain the agreement of each such member country that the proceeds may be exchanged by the Bank for the currency of any other member country without restriction. The Bank's borrowing policy is summarized in **Box 4**.

Box 4: Borrowing Policy

The Bank's policy is to limit the amount of its Net Borrowings to the subscribed callable capital stock of its non-borrowing member countries (the United States, Japan, Canada and the other nonregional members). Net Borrowings is the amount of borrowings plus gross guarantee exposure, less qualified liquid assets and the special reserve assets. Special reserve assets can only be used for meeting the Bank's obligations on borrowings and guarantees. As of December 31, 2006, Net Borrowings represented 57.9% of the subscribed callable capital stock of the non-borrowing member countries compared to 63.5% in 2005.

The objectives of the Bank's borrowing strategy are to secure long-term capital market access, volume and cost effectiveness. The Bank uses derivatives, mostly currency and interest rate swaps, for hedging purposes as part of its liability management to achieve the desired currency composition and interest rate structure as well as to lower its funding costs. The Bank closely monitors and regulates its activities with dealers and counterparties (see "Financial Risk Management—Credit Risk—Commercial Credit Risk" below). The amount and timing of the Bank's borrowings are determined in part by loan disbursements, maturing debt and liquidity levels (see "Liquidity Management" above).

In 2006, the proceeds from medium- and long-term debt raised directly in financial markets amounted to $5.3 billion compared to $4.9 billion in 2005. The increase in 2006 borrowings was primarily attributed to greater flexibility in the Bank's capital markets operations resulting from the new liquidity policy approved in 2005. Borrowing operations for 2006 and 2005 are summarized in **Table 7**.

Table 7: SUMMARY OF ANNUAL BORROWING OPERATIONS
For the years ended December 31, 2006 and 2005
(Amounts expressed in millions of United States dollars)

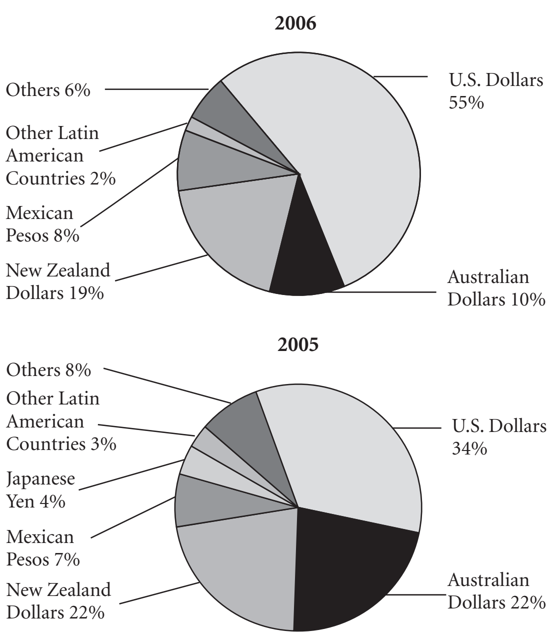
	2006	2005
Total medium- and long-term borrowings(1)	$5,263	$4,922
Average life (years)(2)	6.5	6.3
Number of transactions	33	32
Number of currencies	7	9

(1) Represents proceeds on a trade date basis.
(2) Average life to the first call date.

Borrowings raised in any given year are used for general operations, including loan disbursements and refinancing of maturing debt. In 2006, the Bank issued its first-ever bonds denominated in Peruvian new soles. In addition, the Bank issued two $1 billion global benchmark bonds maturing in 2011 and 2016, respectively. Bonds denominated in borrowing member country currencies in the aggregate amount of $526 million were issued during 2006 (2005—$496 million), comprised of the following currencies: Mexican pesos—$406 million and Peruvian new soles—$120 million (2005—Mexican pesos—$358 million, Colombian pesos—$72 million, and Chilean pesos—$66 million). In addition, the Bank transacted various bonds denominated in Australian dollars, Canadian dollars, New Zealand dollars, South African rand, and United States dollars.

New medium- and long-term borrowings by currency for 2006, as compared to 2005, are shown in **Figure 3**. In 2006, all non-United States dollar borrowings were initially swapped into United States dollars (2005—most swapped into United States dollars and euros).

Figure 3: BORROWINGS BY CURRENCY(1)
For the years ended December 31, 2006 and 2005



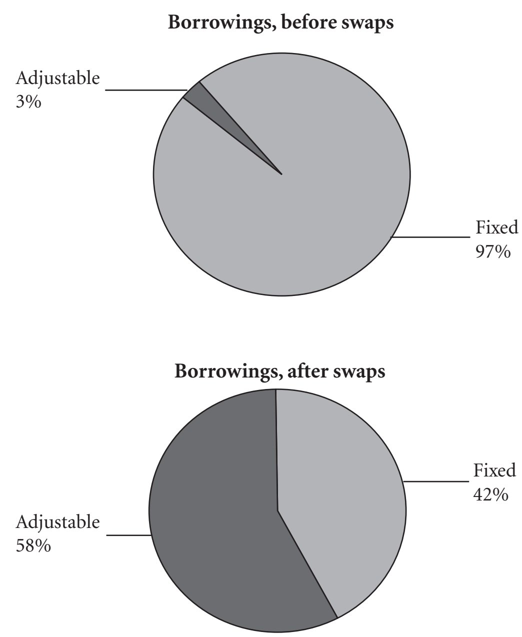
(1) Includes medium- and long-term borrowings, excluding swaps, and represents proceeds on a trade date basis.

The Bank strategically repurchases, calls or prepays its debt to reduce the cost of borrowings and the exposure to refunding requirements in a particular year, or to meet other operational needs. During 2006, the Bank did not call any of its outstanding borrowings compared to $28 million in 2005.

Use of Derivatives: The Bank may enter into currency and interest rate swaps contemporaneously with borrowing transactions in order to convert the proceeds into euro, Japanese yen, Swiss francs or United States dollars and fixed or floating rate funding to meet its loan disbursement obligations. In 2006, almost all of new borrowings were initially swapped into United States dollars at floating rates, with conversion to fixed-rate funding being carried out subsequently in accordance with funding requirements. In addition, as part of the risk mitigation component of the SCF LIBOR-based loan pricing alternative, the Bank purchases caps to reduce its exposure to sudden increases in interest rates. **Figures 4** and **5** illustrate the effect of swaps on both the interest rate structure and currency composition of the medium- and long-term borrowing portfolio at December 31, 2006.

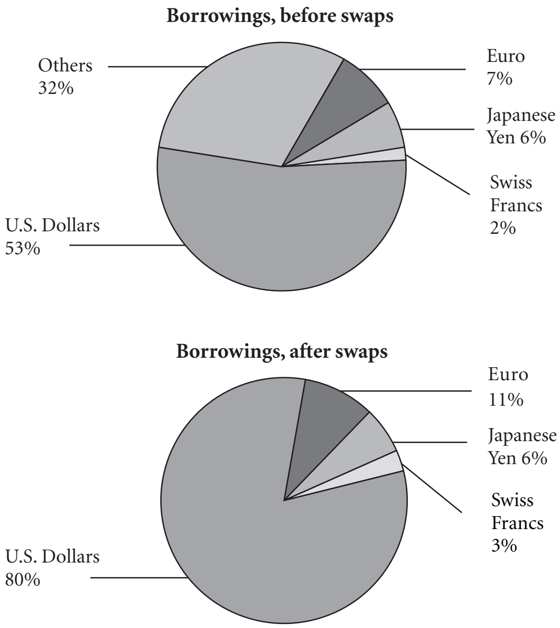
More detailed information with respect to the Bank's borrowings and derivatives is contained in Notes G and H and Appendix I-5 to the financial statements.

Figure 4: EFFECTS OF SWAPS ON INTEREST RATE STRUCTURE OF OUTSTANDING BORROWINGS(1)
December 31, 2006



(1) Medium- and long-term borrowings only.

Figure 5: EFFECTS OF SWAPS ON CURRENCY COMPOSITION OF OUTSTANDING BORROWINGS[1]
December 31, 2006



[1] Medium- and long-term borrowings only.

RESULTS OF OPERATIONS

Operating Income

Operating Income includes the net interest income on earning assets and the income contribution of the Bank's equity, other loan income, the provision (credit) for loan and guarantee losses and net non-interest expense. **Table 8** shows the breakdown of Operating Income during the last three years.

Year 2006 versus 2005: In 2006, Operating Income was $85 million lower than the previous year due to a reduction in the net interest income generated by the loan portfolio and an in-

Table 8: OPERATING INCOME
(Expressed in millions of United States dollars)

	2006	2005	2004
Loan interest income	$2,435	$2,368	$2,446
Investment income	619	403	288
	3,054	2,771	2,734
Less:			
Borrowing expenses	2,070	1,733	1,572
Net interest income	984	1,038	1,162
Other loan income	31	45	52
Other expenses:			
(Credit) provision for loan and guarantee losses	(48)	(14)	21
Net non-interest expense	436	385	331
Total	388	371	352
Operating Income	$ 627	$ 712	$ 862

crease in net non-interest expense, which is chiefly comprised of administrative expenses, partially offset by a higher credit for loan and guarantee losses.

Year 2005 versus 2004: In 2005, Operating Income was $150 million lower than the previous year due to a reduction in the net interest income generated by the loan portfolio and an increase in net non-interest expense, partially offset by a lower provision for loan and guarantee losses.

Net Interest Income

The average interest-earning asset and interest-bearing liability portfolios, after swaps, and the respective returns and costs for 2006, 2005, and 2004 are shown in **Table 9**.

Year 2006 versus 2005: Net interest income decreased $54 million in 2006 with respect to 2005, primarily due to a reduction in emergency loans outstanding (which generate an interest rate margin of 4%) and lower lending spreads on sovereign-guaranteed, non-emergency loans. This decrease was partially offset by an increase in the income generated by the equity resources.

The increase in investment income was primarily due to the overall increase in short-term interest rates during the last

Table 9: ASSET/LIABILITY PORTFOLIOS AND RETURNS/COSTS
(Amounts expressed in millions of United States dollars)

	2006		2005		2004	
	Average Balance	Return/Cost %	Average Balance	Return/Cost %	Average Balance	Return/Cost %
Loans[1]	$47,207	5.16	$47,837	4.95	$49,721	4.92
Liquid investments	14,226	4.39	12,341	3.29	13,415	2.17
Total earning assets	61,433	4.98	60,178	4.61	63,136	4.34
Borrowings	43,314	4.78	42,609	4.07	46,200	3.40
Interest rate spread		0.20		0.54		0.94
Net interest margin[2]		1.60		1.72		1.84

[1] Excludes loan fees.
[2] Represents net interest income as a percent of average earning assets.

two years and an increase in the level of liquid investments held by the Bank. This increase was substantially offset by a corresponding increase in borrowing expenses as LIBOR-based investments (comprising more than three-quarters of the investments) are financed with matching LIBOR-indexed debt.

Year 2005 versus 2004: Net interest income decreased $124 million in 2005 with respect to 2004, primarily due to a reduction in emergency loans outstanding (which generate an interest rate margin of 4%), lower lending spreads on sovereign-guaranteed, non-emergency loans, and a decline in the amount of, and the net interest margin generated by, the Bank's regular loans. This decrease was partially offset by the increase in equity resources and a change in the classification of income collections on non-sovereign-guaranteed loans classified as impaired and/or in nonaccrual status.

Net Non-interest Expense

The main components of net non-interest expense are presented in **Table 10**.

Table 10: NET NON-INTEREST EXPENSE
(Expressed in millions of United States dollars)

	2006	2005	2004
Administrative expenses			
Staff costs	$342	$331	$279
Consultant fees	50	47	44
Operational travel	20	21	19
Other expenses	95	74	62
Total gross administrative expenses	507	473	404
Less: Share of Fund for Special Operations	(93)	(86)	(62)
Net administrative expenses	414	387	342
Service fee revenues	(5)	(6)	(6)
Special programs	34	12	—
Other income	(7)	(8)	(5)
Net non-interest expense	$436	$385	$331

Year 2006 versus 2005: Net non-interest expense increased by $51 million in 2006 mainly due to an increase in depreciation and amortization ($22 million), regular salary and related benefit increases ($11 million) and expenditures under special programs approved by the Board of Executive Directors ($22 million).

Year 2005 versus 2004: Net non-interest expense increased by $54 million in 2005 mainly due to an increase in pension and postretirement benefit costs ($20 million), regular salary and related benefit increases ($11 million), additional employee benefit accruals ($8 million), and expenditures under special programs approved by the Board of Executive Directors ($12 million).

FINANCIAL RISK MANAGEMENT

As part of its development banking services, the Bank is exposed to credit risk (loan portfolio or country credit and commercial credit); market risk (interest rate, spread and exchange rate); liquidity risk (funding and liquidation); and operational risk.

Governance

The Bank conducts its operations within a framework of financial policies, uses only specifically authorized financial instruments and follows a well-defined risk management decision-making process.

The Bank manages its risks in accordance with the Agreement, and such other policies as are approved by its Board of Governors, its Board of Executive Directors and the Finance Committee composed of members of management. Additionally, a Finance Department committee on asset and liability management, chaired by the Finance Manager, develops guidelines and oversees implementation of, and compliance with, the Bank's financial risk management approach in matters of risk, asset and liability management, funding and investments and strategic financial planning.

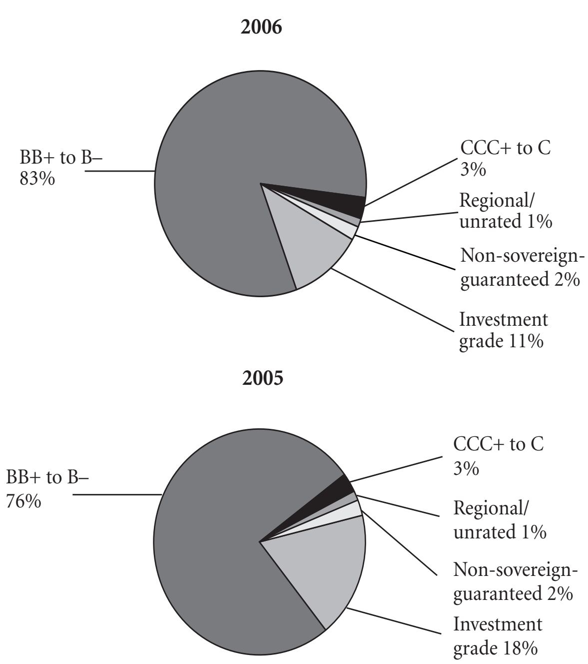
Credit Risk

Credit risk is the potential loss that could result from the default of borrowers (loan portfolio credit risk or country credit risk) or from the default/downgrade of investment, trading or swap counterparties (commercial credit risk). Almost all of the Bank's loans are sovereign-guaranteed.

Loan Portfolio Credit Risk: Loan portfolio credit risk is the risk that the Bank may not receive repayment of principal and/or interest on one or more of its loans according to the agreed-upon terms. It is directly related to the Bank's core business and is the largest financial risk faced by the Bank. The Bank has multiple sources of protection from loan portfolio credit risk, including an overall lending limitation, a comprehensive capital adequacy framework (designed to ensure that the Bank holds sufficient equity at all times given the quality and concentration of its portfolio), a policy for the treatment of non-performing loans and a policy for the maintenance of a loan loss allowance. The Bank's loan portfolio credit risk is determined by the credit quality of, and exposure to, each borrower.

The credit quality of the loan portfolio as of December 31, 2006, as represented by the long-term foreign currency credit ratings assigned to each borrowing country by the rating agencies, is depicted in **Figure 6**. Since December 31, 2005, the effects of ratings upgrades for a number of the Bank's largest borrowers were partially offset by large prepayments by one of the Bank's highest-rated borrowing members, which reduced the percentage of the portfolio rated investment grade, and increased the concentration held by relatively lower-rated countries.

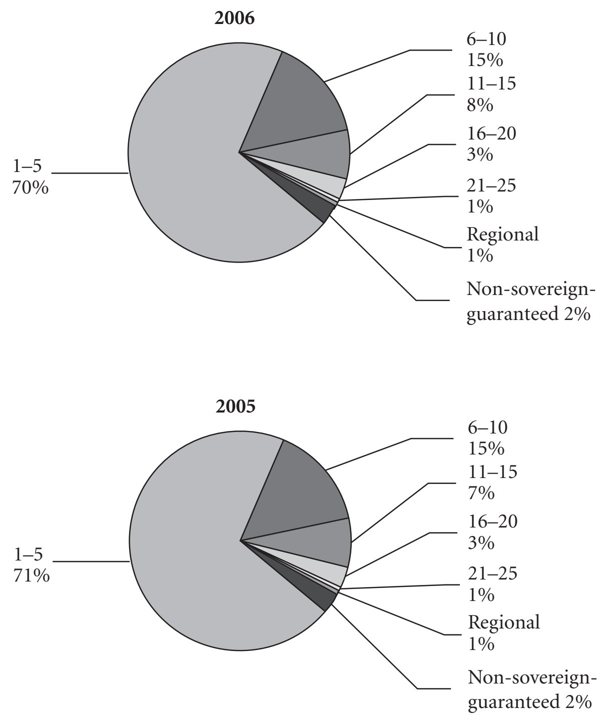
Figure 6: CREDIT QUALITY OF LOAN PORTFOLIO REFLECTED IN RATINGS OF BORROWING MEMBER COUNTRIES
December 31, 2006 and 2005



The Bank's exposure reflects the overall size and concentration of the portfolio. Exposure is limited only by the Bank's lending authority; there are no per-country lending limits. Taking into consideration the regional nature of the Bank's operations and the relative sizes of the economies of its borrowing members, the Bank expects to consistently have a concentrated portfolio. As shown in **Figure 7**, as of December 31, 2006, 70% of the portfolio is held by the five largest borrowers compared to 71% in 2005. Refer to Appendix I-3 to the financial statements for more information.

Lending Limitation: With respect to the overall lending limitation, the Bank's policy is to limit the total amount of outstanding loans and guarantees to its paid-in capital stock plus the general reserve and the callable capital of the non-borrowing member countries. This lending limit is stricter than that prescribed by the Agreement, which also includes the callable capital of the borrowing members.

Figure 7: CONCENTRATION OF LOAN PORTFOLIO
December 31, 2006 and 2005



Capital Adequacy Framework: The capital adequacy framework of the Bank consists of a credit risk model, a policy on capital adequacy and an associated loan pricing methodology. The framework allows the Bank to manage the risk inherent in its loan portfolio due to the credit quality of its borrowers and the concentration of its loans, while also offering its borrowers low and stable loan charges.

The Bank's economic capital is measured by the TELR, whose desired level of 38% was determined based on an analysis of the Bank's economic capital needs under various hypothetical financial stress scenarios. As long as Operating Income is positive and the TELR is increasing within a range between 32% and 38%, the Bank will apply standard loan charges.

Non-performing Loans: Except for non-sovereign-guaranteed loans, loan service delays by a borrower in a member country preclude new loan approvals to borrowers in the member country, may lead to the suspension of loan disbursements, may result in the loan being placed in non-accrual status, and may cause the loan to be declared due and payable. The Bank exercises its policy under a graduated approach as summarized in **Table 11**.

TABLE 11: TREATMENT OF NON-PERFORMING SOVEREIGN-GUARANTEED LOANS

30 days after loan due date	The Bank suspends disbursements on the loan in arrears and all other loans to the borrower. The Bank informs the guarantor of the arrears by the borrower and requests prompt payment of the amount in arrears. No loan contract with a borrower in the country in question is signed by the Bank and no loan proposal is approved.
120 days after loan due date	The Bank suspends disbursements on all loans to the guarantor and guaranteed by the guarantor if the guarantor fails to pay the amounts due.
180 days after loan due date	The Bank places in nonaccrual status all loans for the country in question of which the government, the central bank or any government entity is a borrower or guarantor, unless it is determined that all payments of amounts in arrears are in process and will be collected in the immediate future. Placement in nonaccrual status implies a reversal of all accrued income to date and no further income accumulation until all pending amounts are received. All Bank missions to the country intended for the programming, preparing or processing of loans are suspended.

If loans made to a member country funded with resources of the FSO or of any other fund owned or administered by the Bank are non-performing, all loans made to or guaranteed by that member government are also considered non-performing. The Bank maintains a continuous dialogue with its borrowers to ensure prompt payment on all of its loans.

In the case of non-sovereign-guaranteed loans, an internal Bank committee determines when the loan is classified in nonaccrual status, which can happen anytime between 30 and 90 days of being overdue or, if special circumstances warrant, at any time prior to the expiry of 30 days. At December 31, 2006, all loans were performing, except for certain non-sovereign-guaranteed loans, which were classified as impaired and were in nonaccrual status (see Note E to the financial statements).

Loan and Guarantee Loss Allowances: Because of the nature of its borrowers and guarantors, the Bank expects that each of its Ordinary Capital sovereign-guaranteed loans will be repaid. In addition, the Bank has had an essentially fully performing sovereign-guaranteed loan portfolio since its establishment. During the Bank's 47 years of history, only five borrowing countries have been in nonaccrual, for varying times during 1988–1992. The maximum aggregate balance in nonaccrual never exceeded 8% of total loans outstanding, and the Bank received the full principal and interest due on these loans. The Bank maintains allowances for loan and guarantee losses to recognize the probable losses inherent in its loan and guarantee portfolios, primarily related to non-sovereign-guaranteed operations. Pursuant to Bank policy, a credit for loan and guarantee losses of \$48 million was recognized in income during 2006, for total allowances of \$104 million at December 31, 2006 (2005—\$188 million). At December 31, 2006, the non-sovereign-guaranteed allowances for loan and guarantee losses were 6.7% of the corresponding combined outstanding portfolios (2005—12.3%).

Commercial Credit Risk: Commercial credit risk is the exposure to losses that could result from either the default or the downgrade by a credit rating agency of one of the Bank's investment, trading or swap counterparties. The main sources of commercial credit risk are the financial instruments in which the Bank invests its liquidity. In accordance with its conservative risk policies, the Bank will only invest in high quality debt instruments issued by governments, government agencies, multilateral organizations, financial institutions and corporate entities, including asset-backed securities. The Bank's process for controlling its commercial credit risk includes: a) specifying authorized investments; b) establishing approved lists of acceptable counterparties, issuers and dealers; c) defining acceptable credit rating limits; and d) specifying exposure limits and term limits for acceptable counterparties, issuers and dealers based on their size and creditworthiness.

As part of its regular investment, funding and asset and liability management activities, the Bank uses derivative instruments, primarily swaps, for hedging purposes. The use of derivatives is limited to authorized dealers and counterparties selected on the basis of conservative risk management policies. The Bank has established exposure limits for each derivative counterparty and has entered into master derivative agreements that contain enforceable closeout netting provisions. These agreements also provide for collateralization in the event that the mark-to-market exposure exceeds certain contractual thresholds. Master derivative agreements with derivative counterparties have been amended to make risk mitigation provisions consistent with more conservative levels required under a new derivatives credit risk management policy. Counterparty exposure limits are calculated and monitored on the basis of potential credit exposures modeled throughout the life of each counterparty's portfolio. Simulation is used to model the complex interactions of market risk factors, the dynamics of the portfolio, and the impact of risk mitigation mechanisms such as collateral thresholds and termination triggers, to estimate the potential credit exposure. Monitoring the Bank's exposures and managing such risks are continuous processes. The Bank does not expect nonperformance by any of its counterparties.

The Bank treats current credit exposure as the replacement cost of the relevant derivative instrument. This is also referred to as replacement risk or the mark-to-market exposure amount. Mark-to-market exposure is a measure, at a point in time, of the value of a derivative contract in the open market. When the mark-to-market is positive, it indicates that the counterparty owes the Bank and, therefore, creates an exposure for the Bank. When the mark-to-market is negative, the Bank owes the counterparty and does not have replacement risk. When the Bank has more than one derivative transaction outstanding with a derivative counterparty, the "net" mark-to-market exposure represents the netting of the positive and negative exposures with the same counterparty. If this net mark-to-market is negative, then the Bank's exposure to the counterparty is considered to be zero.

Figure 8 provides details of the estimated credit exposure on investments by issuer rating category. As of December 31, 2006, the credit exposure for the whole investment portfolio amounted to $15.8 billion compared to $13.6 billion at December 31, 2005. The credit quality of the investment portfolio for 2006 continues to be high, as 83% of the issuers were rated AAA and AA, and an additional 8% of the portfolio carried the highest short-term ratings, compared to 85% and 10%, respectively, in 2005. **Figure 9** provides details of the estimated credit exposure (netted by counterparty) on the swap portfolio, by rating category. As of December 31, 2006, the swap credit exposure increased to $1.5 billion from $1.3 billion a year earlier. The credit quality of the swap portfolio continues to be high, as 94% of the counterparties were rated at least AA in 2006, compared to 93% in 2005. These swap credit exposures are collateralized. The 12% exposure to a single AAA counterparty in 2005 was migrated in 2006 to AA counterparties that are required to post collateral. As of December 31, 2006, $1.3 billion of eligible collateral had been posted with the Bank's custodian (compared to $0.9 billion in 2005), which significantly reduced the credit exposure on swaps discussed above to only $0.2 billion (2005—$0.4 billion).

Figure 8: INVESTMENT CREDIT EXPOSURE BY ISSUER RATING
December 31, 2006 and 2005

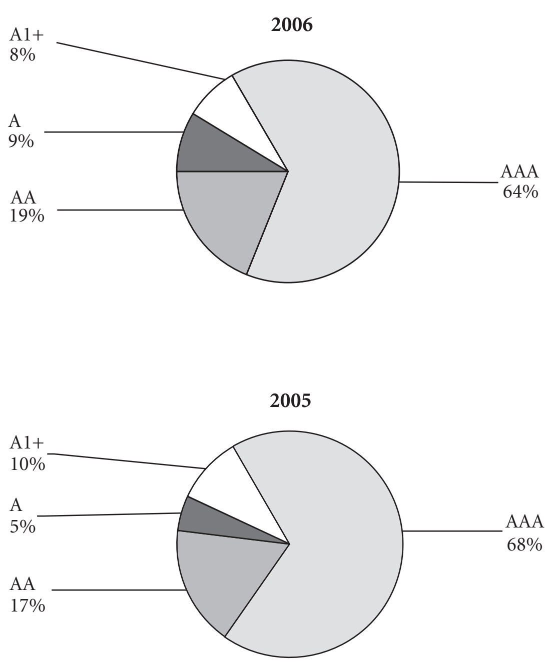
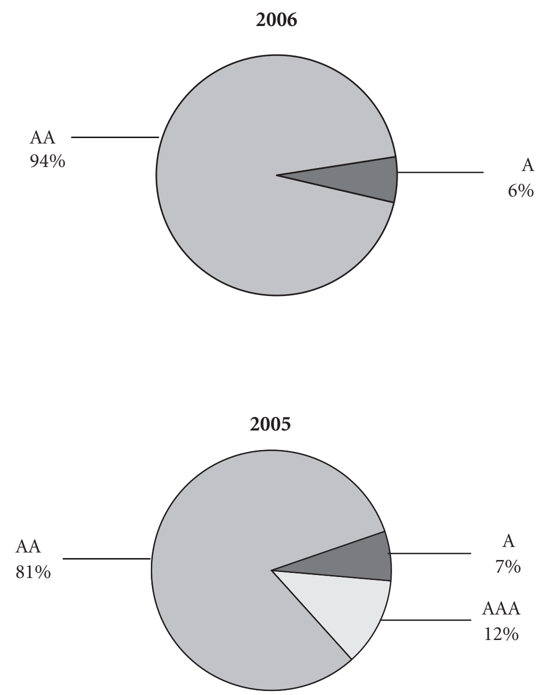


Figure 9: SWAPS CREDIT EXPOSURE BY COUNTERPARTY RATING
December 31, 2006 and 2005



Market Risk

The Bank faces risks that result from market movements, primarily changes in interest and exchange rates. However, exposure to market risks is small as the Bank has an integrated asset and liability management framework.

Asset and Liability Management: The objective of asset and liability management is to ensure adequate funding for each product at the most attractive cost available, and to manage the currency composition, maturity profile and interest rate sensitivity characteristics of the portfolio of liabilities supporting liquidity and each lending product in accordance with the particular requirements for that product and within prescribed risk parameters. The Bank employs derivatives to manage and align the characteristics of its assets and liabilities, enhance investment returns and lower borrowing costs.

Interest Rate Risk: The Bank is exposed to two potential sources of interest rate risk. The first is the exposure to changes in the net spread between the rate earned on assets and the cost of borrowings that fund those assets. The second is the exposure to changes in the income earned on the portion of the assets funded with equity.

The Bank mitigates its exposure to net spread changes through a cost pass-through formulation incorporated in the lending rates charged on most of its existing loans, in addition to a carefully designed term structure management. These cost pass-through loans account for 91.1% of the existing outstanding loan portfolio as of December 31, 2006; the remaining 8.9% are emergency loans, non-sovereign-guaranteed loans and fixed-rate loans. Some of the cost pass-through loans, primarily the adjustable rate loans, pose some residual interest rate risk given the six-month lag inherent in the lending rate calculation (see "Development Operations—Financial Terms of Loans" above). The Bank funds and invests its liquidity at matching rate structures using specific duration gap constraints, thus avoiding any undue exposure to interest rate risk.

The Bank mitigates its exposure to equity-induced income changes by investing these funds in long-term loan and investment assets, with stable returns.

Exchange Rate Risk: In order to minimize exchange rate risk in a multicurrency environment, the Bank matches the after-swap borrowing obligations in any one currency with assets in the same currency, as prescribed by the Agreement. In addition, the Bank's policy is to minimize the exchange rate sensitivity of its TELR by performing periodic currency conversions to maintain the currencies underlying its equity and allowances for loan and guarantee losses aligned with those of the outstanding loans and net guarantee exposure. In order to minimize currency misalignments, the Bank also aligns the currency composition of the special reserve assets with that of its outstanding borrowings.

Figure 10 presents the currency composition of the Bank's assets and liabilities (after swaps) at the end of 2006 and 2005.

Liquidity Risk

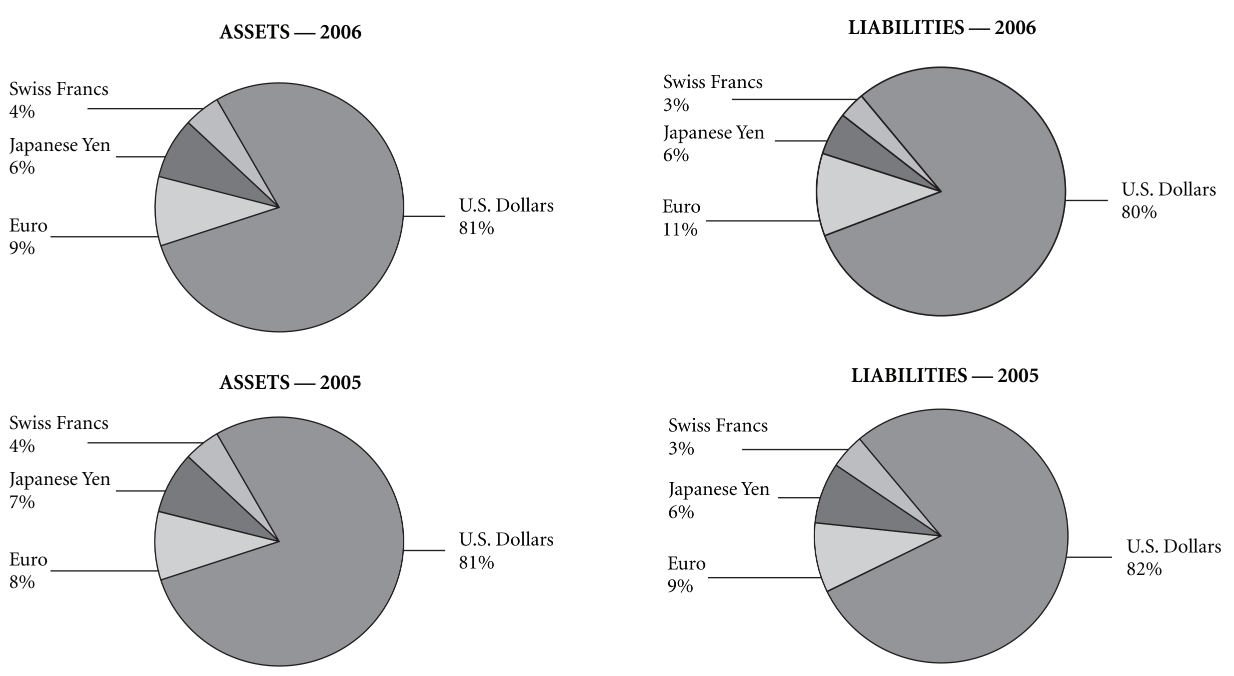
Liquidity risk arises from the general funding needs of the Bank's activities and in the management of its assets and liabilities. It includes the risk of being unable to fund the portfolio of assets at appropriate maturities and rates (funding risk); the risk of being unable to liquidate a position in a timely manner at a reasonable price (liquidation risk); and the exacerbation of these two risks by having significant portions of a portfolio of assets or liabilities allocated to a specific type of instrument (concentration risk).

The Bank manages liquidity risk through its liquidity policy, asset-liability management policy and its short-term borrowing program. The Bank's liquidity policy determines a minimum amount of liquidity, which is designed to allow the Bank to refrain from borrowing for a period of time while continuing to meet its own obligations. The asset and liability management of the Bank, in addition to optimizing the allocation of equity and debt to fund the Bank's various assets, determines the proper term-duration gap between loans and debt to both lower funding costs and reduce refunding risk. Finally, under the short-term borrowing program, discount notes with maturities of less than one year are issued to cover short-term cash flow needs whenever the liquidation of a position is not desirable.

Operational Risk

Operational risk is the potential loss arising from internal activities or external events, caused by breakdowns in information, communication, physical safeguards, business continuity, supervision, transactions processing, pricing, cash and securi-

Figure 10: CURRENCY COMPOSITION OF ASSETS & LIABILITIES
December 31, 2006 and 2005



ties movements and settlement systems. In addition, operational risk includes fraud and failures in the execution of legal, fiduciary and agency responsibilities.

Within the Bank there are policies and procedures in place covering all significant aspects of operational risk. These include first and foremost the Bank's high standards of business ethics and its established system of internal controls. These are supplemented by the Bank's disaster recovery/contingency planning, the Information Disclosure Policy, client and project integrity due diligence procedures, and procurement and purchasing policies.

Internal Control Over Financial Reporting: During 2006, the Bank implemented the Committee of Sponsoring Organizations of the Treadway Commission (COSO) Internal Control-Integrated Framework for its financial reporting, and established an annual process for management to report on the effectiveness of the internal control over financial reporting, and for the external auditors to attest as to the accuracy of management's assessment and the effectiveness of the internal control over financial reporting. The first management's assessment report and external auditors' attestation were performed for financial information as of December 31, 2006, and are included in the financial statements of the Ordinary Capital.

ADDITIONAL REPORTING AND DISCLOSURE

Basis of Reporting

The financial statements are prepared in accordance with United States generally accepted accounting principles (GAAP), which require management to make estimates and assumptions that affect the reported results (see Note B to the financial statements).

Critical Accounting Policies

The Bank believes that some of the more significant accounting policies it uses to present its financial results in accordance with GAAP involve a relatively high degree of judgment and complexity and relate to matters that are inherently uncertain.

Fair Value of Financial Instruments: The Bank uses fair value estimates to account for the trading investments portfolio and all derivatives (mostly interest and currency swaps), and for disclosures of financial instruments. Until December 31, 2003, the Bank also used fair value estimates to determine adjustments to the carrying amounts of hedged loans and borrowings designated in hedge accounting relationships (namely the loan and bond fair value adjustments, respectively). Fair values are based on market prices when they are available. If market quotes are not available, fair values are based on dealer prices, prices of comparable instruments or discounted cash flows using pricing models. Pricing models use inputs from market sources such as interest rate yield curves, currency exchange rates and option volatility. These assumptions may have a significant effect on the reported fair values of assets and liabilities (including derivatives) and related income and expenses. Management believes its estimates of fair value are reasonable given its processes for obtaining external prices and parameters and the consistent application of this approach from period to period.

Changes in the fair value of trading securities and related derivatives are presented in Income from investments on the Statement of Income and Retained Earnings. Changes in the fair value of all derivatives other than investment derivatives and, up to December 31, 2003, of those assets and liabilities linked to derivatives and designated as fair value hedges in accordance with SFAS 133, are reported in Effects of SFAS 133 and currency transaction adjustments. See "Effects of SFAS 133 and Currency Transaction Adjustments" below.

Loan and Guarantee Loss Allowances: The Bank maintains allowances for losses on its loan and guarantee portfolios at levels management believes to be adequate to absorb estimated losses inherent in the total portfolio at the balance sheet date. Setting the level of the allowances requires significant judgment. The use of different estimates or assumptions as well as changes in external factors could produce materially different provisions and allowance levels. Because of the nature of its borrowers and guarantors, the Bank expects that each of its sovereign-guaranteed loans will be repaid. Accordingly, the level of its loan and guarantee loss allowances is relatively small and mainly related to the non-sovereign-guaranteed loan portfolio.

Pension and Other Postretirement Benefits: The Bank participates along with the Inter-American Investment Corporation (IIC) in pension and postretirement benefit plans that cover substantially all of their staff members. All costs, assets and liabilities associated with the plans are allocated between the Bank and the IIC based upon their employees' respective participation in the plans. Costs allocated to the Bank are subsequently shared between the Ordinary Capital and the FSO based on a cost allocation ratio approved by the Board of Executive Directors. The underlying actuarial assumptions used to determine the projected benefit obligations, fair value of plan assets and funded status associated with these plans are based on financial market interest rates, past experience, and management's best estimate of future benefit changes and economic conditions. For further details, refer to Note M to the financial statements.

Effects of SFAS 133 and Currency Transaction Adjustments

As required by SFAS 133, the Bank marks to market all derivative instruments with changes in fair value recognized in income. Up to December 31, 2003, the Bank designated in hedging relationships most of the derivatives related to its borrowing and lending activities, following the SFAS 133 criteria. Accordingly, changes in the fair values of hedged assets and liabilities were also recognized in income, substantially offsetting the derivatives mark to market adjustments in previous years. The changes in fair value of both the derivative instrument and the underlying borrowing included changes in fair value due to changes in exchange rates, which offset each other almost entirely under hedge accounting.

Effective January 1, 2004, the Bank elected to discontinue hedge accounting for all its SFAS 133 hedging relationships while continuing to measure all derivatives at fair value, with changes in fair value recognized in income. In addition, the effect of exchange rate changes that had been included in the borrowings' fair value adjustments is now recognized as currency transaction adjustments. Management considers that these two elements are economically related and hence are reported together in a separate line in the Statement of Income and Retained Earnings.

The discontinuation of hedge accounting required the Bank to start amortizing the previously recorded fair value adjustments on borrowings and loans. In addition, the Bank's current application of SFAS 133 requires that only derivative instruments be marked to market. During 2006, the amortization of fair value adjustments on borrowings and loans, the net impact of exchange rates on borrowing transactions, and the impact of interest rates on borrowing and lending swaps amounted to an increase (decrease) in income of $62 million, $30 million, and ($469) million, respectively (2005—$85 million, ($32) million, and $5 million, respectively; 2004—$250 million, $27 million, $48 million, respectively) (for additional information, see Note H to the financial statements). As a result, Effects of SFAS 133 and currency transaction adjustments has been substantially higher after the discontinuation of hedge accounting in 2004 (negative $384 million in 2006 and positive $50 million and $314 million in 2005 and 2004, respectively). Management believes that this reported income volatility is not representative of the underlying economics of the transactions as the Bank generally holds its swaps to maturity.

External Auditors

General: The external auditors are appointed by the Board of Governors following a competitive bidding process. In 2002, Ernst & Young LLP (E&Y) was appointed as external auditors. Pursuant to an agreement between the Bank and E&Y, the parties extended, on a yearly basis through 2006, E&Y's appointment. The Bank is currently carrying out a competitive bidding to appoint the external auditors for the five-year period 2007–2011.

Contracted fees for audit services provided to the Bank by E&Y in connection with the 2006 financial statement and internal control audits amount to $940,000. In addition, E&Y was paid $117,000 during 2006 for services related to bond issuance and advisory services related to the implementation of the COSO Internal Control-Integrated Framework. E&Y also provides audit services to trust funds administered by the Bank and to the Bank's staff retirement plans. Contracted fees expected to be paid for services related to the 2006 audits of such trust funds and plans amount to $474,000.

External Auditors' Independence: The Audit Committee is responsible for, among other matters, assisting the Board of Executive Directors in overseeing the external audit function, including ensuring external auditors' independence. In this regard, the Committee is guided by the following key principles:

- The work plan of the external auditors, including audit and audit-related services, must be approved by the Board of Executive Directors, based on the recommendation of the Audit Committee.
- Any other services to be performed by the external auditors on an exceptional basis may be hired by management following criteria established by the Audit Committee.
- The external auditors' engagement and review partners must rotate at least every five years.
- The performance of the external auditors is evaluated annually.
- The external auditors' independence must be confirmed annually by the Audit Committee.
- The external auditors have full access to the Audit Committee and the Board of Executive Directors.

FINANCIAL STATEMENTS

ORDINARY CAPITAL

MANAGEMENT'S REPORT REGARDING THE EFFECTIVENESS OF INTERNAL CONTROL OVER FINANCIAL REPORTING

February 6, 2007

The Management of the Inter-American Development Bank (Bank) is responsible for establishing and maintaining effective internal control over financial reporting in the Bank. Management has evaluated the Bank's Ordinary Capital internal control over financial reporting using the criteria for effective internal control established in the Internal Control–Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Management has assessed the effectiveness of the Bank's Ordinary Capital internal control over financial reporting as of December 31, 2006. Based on this assessment, Management believes that the Bank's internal control over financial reporting is effective as of December 31, 2006.

There are inherent limitations in the effectiveness of any internal control system, including the possibility of human error and the circumvention or overriding of controls. Accordingly, even an effective internal control can provide only reasonable assurance with respect to financial statement preparation. Further, because of changes in conditions, the effectiveness of internal control may vary over time.

The Bank's Ordinary Capital financial statements, as of December 31, 2006, have been audited by Ernst & Young LLP, an independent registered public accounting firm. Ernst & Young LLP has also issued an attestation report on management's assessment of the Bank's Ordinary Capital internal control over financial reporting.

Luis Alberto Moreno
President

Ciro De Falco
Vice President for Finance and Administration

John R. Hauge
Finance Department Manager

REPORT OF INDEPENDENT AUDITORS

Board of Governors
Inter-American Development Bank

We have audited management's assessment, included in the accompanying Management's Report Regarding the Effectiveness of Internal Control over Financial Reporting, that the Inter-American Development Bank (Bank)—Ordinary Capital maintained effective internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control–Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). The Bank's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Bank's Ordinary Capital internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over external financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that the Bank's Ordinary Capital maintained effective internal control over financial reporting as of December 31, 2006, is fairly stated, in all material respects, based on the COSO criteria. Also, in our opinion, the Bank maintained, in all material respects, effective internal control over financial reporting as of December 31, 2006, based on the COSO criteria**.**

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the balance sheet of the Inter-American Development Bank—Ordinary Capital as of December 31, 2006 and 2005, and the related statements of income and retained earnings, comprehensive income, and cash flows for each of the three years in the period ended December 31, 2006 and our report dated February 6, 2007 expressed an unqualified opinion thereon.

Ernst + Young LLP

Washington, D.C.
February 6, 2007

REPORT OF INDEPENDENT AUDITORS

Board of Governors
Inter-American Development Bank

We have audited the accompanying balance sheet of the Inter-American Development Bank (Bank)—Ordinary Capital as of December 31, 2006 and 2005, and the related statements of income and retained earnings, comprehensive income, and cash flows for each of the three years in the period ended December 31, 2006. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform an audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Inter-American Development Bank—Ordinary Capital as of December 31, 2006 and 2005, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2006, in conformity with United States generally accepted accounting principles.

As discussed in Note B to the financial statements, in 2006 the Bank adopted Statement of Financial Accounting Standards 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans".

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Bank's Ordinary Capital internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 6, 2007 expressed an unqualified opinion thereon.

Ernst + Young LLP

Washington, D.C.
February 6, 2007

ORDINARY CAPITAL
INTER-AMERICAN DEVELOPMENT BANK

BALANCE SHEET

Expressed in millions of United States dollars

	December 31, 2006		December 31, 2005	
ASSETS				
Cash and investments				
Cash	$ 276		$ 223	
Investments				
Trading	12,278		10,183	
Held-to-maturity	3,543	$16,097	3,414	$13,820
Loans outstanding	45,932		48,135	
Allowance for loan losses	(90)	45,842	(175)	47,960
Accrued interest and other charges				
On investments	95		85	
On loans	594		587	
On swaps, net	25	714	73	745
Receivable from members				
Non-negotiable, non-interest-bearing demand obligations	361		370	
Amounts required to maintain value of currency holdings	57	418	73	443
Currency and interest rate swaps				
Investments—trading	2		3	
Loans	5		5	
Borrowings	1,880	1,887	1,596	1,604
Other assets				
Postretirement benefit assets	863		186	
Property, net	301		326	
Unamortized borrowing costs	196		218	
Miscellaneous	157	1,517	80	810
Total assets		$66,475		$65,382
LIABILITIES AND EQUITY				
Liabilities				
Borrowings				
Short-term	$ 658		$ 926	
Medium- and long-term	44,030	$44,688	44,167	$45,093
Currency and interest rate swaps				
Investments—trading	1		61	
Loans	9		10	
Borrowings	742	752	491	562
Payable for investment securities purchased		47		45
Amounts payable to maintain value of currency holdings		315		188
Accrued interest on borrowings		586		607
Accounts payable and accrued expenses		279		160
Total liabilities		46,667		46,655
Equity				
Capital stock				
Subscribed 8,368,563 shares	100,953		100,953	
Less callable portion	(96,613)		(96,613)	
Paid-in capital stock	4,340		4,340	
Retained earnings	14,442		14,199	
Accumulated other comprehensive income	1,026	19,808	188	18,727
Total liabilities and equity		$66,475		$65,382

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

ORDINARY CAPITAL
INTER-AMERICAN DEVELOPMENT BANK

STATEMENT OF INCOME AND RETAINED EARNINGS

Expressed in millions of United States dollars

	Years ended December 31,		
	2006	**2005**	**2004**
Income			
Loans			
Interest	**$ 2,435**	$ 2,368	$ 2,446
Other loan income	**31**	45	52
	2,466	2,413	2,498
Investments	**619**	403	288
Other	**12**	14	11
Total income	**3,097**	2,830	2,797
Expenses			
Borrowing expenses			
Interest, after swaps	**2,015**	1,678	1,526
Amortization of borrowing costs	**55**	55	46
	2,070	1,733	1,572
(Credit) provision for loan and guarantee losses	**(48)**	(14)	21
Administrative expenses	**414**	387	342
Special programs	**34**	12	—
Total expenses	**2,470**	2,118	1,935
Income before SFAS 133 and currency transaction adjustments	**627**	712	862
Effects of SFAS 133 and currency transaction adjustments	**(384)**	50	314
Net income	**243**	762	1,176
Allocation to the Fund for Special Operations	**—**	—	(27)
Addition to Retained earnings for the year	**243**	762	1,149
Retained earnings, beginning of year	**14,199**	13,437	12,288
Retained earnings, end of year	**$14,442**	$14,199	$13,437

STATEMENT OF COMPREHENSIVE INCOME

Expressed in millions of United States dollars

	Years ended December 31,		
	2006	**2005**	**2004**
Net income	**$243**	$ 762	$1,176
Other comprehensive income			
Translation adjustments	**149**	(554)	239
Reclassification to income—cash flow hedges	**8**	8	11
Total other comprehensive income (loss)	**157**	(546)	250
Comprehensive income	**$400**	$ 216	$1,426

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

ORDINARY CAPITAL
INTER-AMERICAN DEVELOPMENT BANK

STATEMENT OF CASH FLOWS

Expressed in millions of United States dollars

	Years ended December 31,		
	2006	**2005**	**2004**
Cash flows from lending and investing activities			
Lending:			
Loan disbursements (net of participations)	**$ (6,088)**	$ (4,899)	$ (3,768)
Loan collections (net of participations)	**8,615**	5,224	5,199
Loan recoveries	**3**	9	—
Net cash provided by lending activities	**2,530**	334	1,431
Gross purchases of held-to-maturity investments	**(2,049)**	(2,392)	(4,448)
Gross proceeds from maturities of held-to-maturity investments	**2,056**	2,531	4,420
Purchase of property	**(15)**	(24)	(34)
Miscellaneous assets and liabilities	**7**	(6)	17
Net cash provided by lending and investing activities	**2,529**	443	1,386
Cash flows from financing activities			
Medium- and long-term borrowings:			
Proceeds from issuance	**5,276**	5,039	4,519
Repayments	**(6,510)**	(5,711)	(7,798)
Short-term borrowings:			
Proceeds from issuance	**10,276**	8,602	6,059
Repayments	**(10,559)**	(7,969)	(7,325)
Collections of receivable from members	**12**	26	35
Net cash used in financing activities	**(1,505)**	(13)	(4,510)
Cash flows from operating activities			
Gross purchases of trading investments	**(20,468)**	(14,670)	(15,901)
Gross proceeds from sale or maturity of trading investments	**18,672**	13,329	17,977
Loan income collections	**2,457**	2,405	2,426
Interest and other costs of borrowings, after swaps	**(1,857)**	(1,544)	(1,412)
Income from investments	**588**	395	273
Other income	**13**	14	10
Administrative expenses	**(367)**	(335)	(352)
Special programs	**(7)**	(1)	—
Net cash (used in) provided by operating activities	**(969)**	(407)	3,021
Cash allocation to the Fund for Special Operations	**—**	—	(27)
Effect of exchange rate fluctuations on cash	**(2)**	(10)	(7)
Net increase (decrease) in Cash	**53**	13	(137)
Cash, beginning of year	**223**	210	347
Cash, end of year	**$ 276**	$ 223	$ 210

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

ORDINARY CAPITAL
INTER-AMERICAN DEVELOPMENT BANK

NOTES TO FINANCIAL STATEMENTS

Note A – Origin
The Inter-American Development Bank (Bank) is an international organization which was established in December 1959. Its purpose is to promote the economic and social development of Latin America and the Caribbean, primarily by providing loans and related technical assistance for specific projects and for programs of economic reform. The primary activities of the Bank are conducted through the Ordinary Capital, which is supplemented by the Fund for Special Operations (FSO) and the Intermediate Financing Facility Account (IFF). The FSO was established to make loans on highly concessional terms in the less developed member countries of the Bank. The IFF's purpose is to subsidize part of the interest payments for which certain borrowers are liable on loans from the Ordinary Capital.

Note B – Summary of Significant Accounting Policies
The financial statements are prepared in conformity with United States generally accepted accounting principles (GAAP). The preparation of such financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. Significant judgments have been made in the valuation of certain financial instruments, the determination of the adequacy of the allowances for loan and guarantee losses, and the determination of the projected benefit obligations of the pension and postretirement benefit plans, the fair value of plan assets and the funded status and net periodic benefit cost associated with these plans.

New accounting pronouncements
In February 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) 155 "Accounting for Certain Hybrid Financial Instruments", an amendment of SFAS 133 and SFAS 140, which, among other provisions, permits fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation. The Bank adopted this pronouncement effective January 1, 2006, as allowed by the corresponding transition provisions. In view of the small number of hybrid financial instruments issued or acquired by the Bank, the effect of implementing SFAS 155 was not significant on the Bank's financial position and results of operations.

In September 2006, the FASB issued SFAS 157 "Fair Value Measurements", which defines fair value, establishes a framework for measuring fair value under GAAP, and expands disclosures about fair value measurements. For the Bank, SFAS 157 will be effective for the 2008 financial statements. Management believes that the provisions of this standard will not have a material impact on the Bank's financial position and results of operations.

Also in September 2006, the FASB issued SFAS 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans", which requires employers with single-employer defined benefit pension, retiree healthcare and other postretirement plans to fully recognize in their statement of financial position an asset for a plan's overfunded status or a liability for a plan's underfunded status through comprehensive income, as well as to measure its funded status (i.e., the difference between the plan assets and obligations) as of the end of the year. The Bank adopted SFAS 158 in 2006. Accordingly, the accompanying Balance Sheet includes the overfunded status of the Bank's pension and postretirement benefit plans as of December 31, 2006. Note M to the financial statements discloses the incremental effect of applying this standard on the individual line items in the year-end Balance Sheet.

Translation of currencies
The financial statements are expressed in United States dollars; however, the Bank conducts its operations in the currencies of all of its members, which are considered functional currencies to the extent that the operations are conducted in those currencies. The Ordinary Capital resources are derived from capital stock, borrowings and accumulated earnings in those various currencies. Assets and liabilities in functional currencies are translated into United States dollars at market exchange rates prevailing at the Balance Sheet dates. Except for currency holdings derived from paid-in capital stock, that have maintenance of value as described below, net adjustments resulting from the translation of functional currencies are charged or credited to Translation adjustments[1], and are presented as a separate component of Other comprehensive income in the Statement of Comprehensive Income. Borrowings in non-functional currencies are translated with the gain or loss recorded in Effects of SFAS 133 and currency transaction adjustments on the Statement of Income and Retained Earnings. Income and expenses are translated at market exchange rates prevailing during each month.

Valuation of capital stock
The Agreement Establishing the Inter-American Development Bank (Agreement) provides that capital stock be expressed in terms of the United States dollar of the weight and fineness in

[1] References to captions in the financial statements are identified by the name of the caption beginning with a capital letter every time they appear in the notes to the financial statements.

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NOTES TO FINANCIAL STATEMENTS (continued)

effect on January 1, 1959. The Second Amendment to the Articles of Agreement of the International Monetary Fund eliminated par values of currencies in terms of gold effective April 1, 1978. Consequently, the General Counsel of the Bank rendered an opinion that the Special Drawing Right (SDR) became the successor to the 1959 United States dollar as the standard of value for the Bank's capital stock, and for maintaining the value of its currency holdings. The SDR has a value equal to the sum of the values of specific amounts of stated currencies, including the United States dollar. Pending a decision by the Bank's governing boards and as suggested in the General Counsel's opinion, the Bank is continuing its practice of using as the basis of valuation the 1959 United States dollar, as valued in terms of United States dollars at July 1, 1974, whose value is equal to approximately 1.2063 of the then current United States dollars.

Maintenance of value (MOV)
In accordance with the Agreement, each member is required to maintain the value of its currency held in the Ordinary Capital, except for currency derived from borrowings. Likewise, the Bank is required to return to a member an amount of its currency equal to any significant increase in value of such member's currency so held, except for currency derived from borrowings. The standard of value for these purposes is the United States dollar of the weight and fineness in effect on January 1, 1959.

The amount related to MOV on non-borrowing member countries' currency holdings is presented as an asset or liability on the Balance Sheet, included in Amounts required/payable to maintain value of currency holdings.

Retained earnings
Retained earnings comprise the general reserve and the special reserve. The general reserve consists of income from prior years, which have been retained for the Bank's operations. In accordance with resolutions of the Board of Governors, net income is generally added to the general reserve to provide for possible annual excess of expenses over income.

The special reserve consists of loan commissions set aside pursuant to the Agreement, which are held in investments. These investments may be used only for the purpose of meeting liabilities on borrowings and guarantees in the event of defaults on loans made, participated in, or guaranteed with resources of the Ordinary Capital. The allocation of such commissions to the special reserve was discontinued in 1998 and no further additions are being made to it.

Investments
Investment securities are classified based on management's intention on the date of purchase, and are recorded using trade-date accounting. Securities which management has the intent and ability to hold until maturity are included in the held-to-maturity portfolio and reported at amortized cost. All other securities are held in a trading portfolio. Securities and related derivative instruments (mostly currency and interest rate swaps) held in the trading portfolio are carried and reported at fair value, with changes in fair value included in Income from investments on the Statement of Income and Retained Earnings.

Loans
The Bank makes loans to its developing member countries, agencies or political subdivisions of such members and to private enterprises carrying out projects in their territories. In the case of loans to borrowers other than national governments, central banks or other governmental or inter-governmental entities, the Bank follows the general policy of requiring a guarantee engaging the full faith and credit of the government. Up to 10% of the outstanding loans and guarantees, not including emergency lending, may be made directly to private sector or (as of August 2006) sub-sovereign entities ("eligible entities") without a sovereign guarantee ("non-sovereign-guaranteed operations") on the basis of market based pricing. These financings are subject to certain prudential limits, including a ceiling on financing the lesser of $200 million or 50% of the total project cost for expansion projects and credit guarantees, subject to such financing not exceeding 25% (certain countries 40%) of an entity's total capitalization of debt and equity, and 25% of the total project cost (certain countries 40%) for new projects. The Bank can also provide political risk guarantees of up to the lesser of $200 million or 50% of the total project cost. In exceptional circumstances, the Board of Executive Directors may approve financings of up to $400 million. In addition, the Bank's maximum exposure to any single obligor for non-sovereign-guaranteed operations cannot exceed 2.5% of the Bank's equity at the time of approval.

Loans representing approximately 35% of the outstanding balances have repayment obligations in various currencies determined on the basis of a currency pooling system (CPS). The principal amount of CPS loans is repayable, in aggregate, in the currencies lent. Single currency loans are repayable in the specific currencies disbursed.

Incremental direct costs associated with originating loans are expensed as incurred as such amounts are considered immaterial to the financial results. Front-end fees on emergency loans are deferred and amortized over the first four years of the loan on a straight-line basis, which approximates the effective interest method.

Income on loans is recognized following the accrual basis of accounting. It is the policy of the Bank to place on nonac-

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crual status all loans made to, or guaranteed by, a member of the Bank if principal, interest or other charges with respect to any such loan are overdue by more than 180 days. In addition, if loans made to a member country with resources of the FSO or of any other fund owned or administered by the Bank are placed on nonaccrual status, all Ordinary Capital loans made to, or guaranteed by, that member government will also be placed on nonaccrual status. On the date a member's loans are placed on nonaccrual status, unpaid interest and other charges accrued on loans outstanding to the member are deducted from the income of the current period. Interest and other charges on nonaccruing loans are included in income only to the extent that payments have actually been received by the Bank. On the date a member pays in full all overdue amounts, the member's loans emerge from nonaccrual status, its eligibility for new loans is restored and all overdue charges (including those from prior years) are recognized as income from loans in the current period.

For non-sovereign-guaranteed loans, it is the policy of the Bank to place on nonaccrual status loans made to a borrower when interest or other charges are past due by more than 90 days, or earlier when management has doubts about the future collectibility of principal or interest. Income is recorded thereafter on a cash basis until loan service is current and management's doubts about future collectibility cease to exist. If the collectibility risk is considered to be particularly high at the time of arrears clearance, the borrower's loans may not emerge from nonaccrual status.

The Bank considers a non-sovereign-guaranteed loan as impaired when, based on current information and events, it is probable that the Bank will be unable to collect all amounts due according to the loan's original contractual terms. Specific allowances for losses on impaired loans are set aside based on management's judgment of the present value of expected future cash flows discounted at the loan's effective interest rate or based on the fair value of the collateral. Income on impaired loans is recognized on a cash basis.

The Bank does not reschedule sovereign-guaranteed loans and has not written off any such Ordinary Capital loans. The Bank periodically reviews the collectibility of loans and guarantees and, if applicable, records, as an expense, provisions for loan and guarantee losses in accordance with its determination of the collectibility risk of the total loan and guarantees portfolio. Such reviews consider the probabilities of default associated with the external credit ratings of each individual borrower, adjusted to reflect the probability of default to the Bank, as well as the potential for loss arising from delay in the scheduled loan repayments. Because of the nature of its borrowers and guarantors, the Bank expects that each of its sovereign-guaranteed loans will be repaid.

Guarantees

The Bank may make partial political risk and partial credit guarantees either without a sovereign counter-guarantee under the 10% limit established for non-sovereign-guaranteed operations, or with a member country sovereign counter-guarantee. As part of its non-sovereign-guaranteed lending activities, the Bank has issued partial political risk and partial credit guarantees designed to encourage private sector infrastructure investments, local capital market development, and trade finance. The partial political risk guarantees and partial credit guarantees may be offered on a stand-alone basis or in conjunction with a Bank loan. Partial political risk guarantees cover specific risk events related to non-commercial factors (such as currency convertibility, transferability of currencies outside the host country, and government non-performance). Partial credit guarantees cover payment risks for debt obligations or trade-finance transactions. The terms of all guarantees are specifically set in each guarantee agreement and are primarily tied to a project, the terms of debt issuances or trade-finance transactions. On a case-by-case basis, depending upon the risks covered and the nature of each individual project, the Bank may reinsure certain guarantees to reduce its exposure. Guarantee fees, net of reinsurance premiums, are charged and recognized as income over the term of the guarantee.

Guarantees are regarded as outstanding when the borrower incurs the underlying financial obligation and are called when a guaranteed party demands payment under the guarantee. The outstanding amount represents the maximum potential risk if the payments guaranteed for these entities are not made. The contingent liability for probable losses related to guarantees outstanding is included in Accounts payable and accrued expenses.

Receivable from members

Receivable from members includes non-negotiable, non-interest-bearing demand obligations that have been accepted in lieu of the immediate payment of all or any part of a member's subscribed paid-in capital stock and MOV obligations.

Property

Property is recorded at cost. Major improvements are capitalized while routine replacements, maintenance and repairs are charged to expense. Depreciation is computed on the straight-line method over estimated useful lives (30 to 40 years for buildings, 10 years for building improvements and capitalized software, and 5 to 15 years for equipment).

Borrowings

To ensure funds are available for its lending and liquidity operations, the Bank borrows in the international capital markets, offering its debt securities to private and public investors. The Bank issues debt securities denominated in various currencies and with various maturities, formats, and structures. The Bank also issues short-term discount notes for liquidity management purposes. Substantially all borrowings are carried on the Balance Sheet at their par value (face value), adjusted for any unamortized SFAS 133 fair value adjustments, premiums or discounts. The amortizations of SFAS 133 fair value adjustments and premiums or discounts are calculated following a methodology that approximates the effective interest method, and are included in Effects of SFAS 133 and currency transaction adjustments and in Interest under Borrowing expenses, respectively, on the Statement of Income and Retained Earnings. Borrowing costs associated with a bond offering are deferred and amortized on a straight-line basis (which approximates the effective interest method) over the life of the respective debt security. The unamortized balance of the borrowing costs is presented separately under Other assets on the Balance Sheet, and the amortization is presented as a separate element under Borrowing expenses on the Statement of Income and Retained Earnings.

Derivatives
As part of its asset and liability management, the Bank uses derivatives, mostly currency and interest rate swaps, in its investment, loan and borrowing operations. These derivatives modify the interest rate and/or currency characteristics of the respective operation to produce the desired interest and/or currency type.

The Bank complies with the derivative accounting requirements of SFAS 133 "Accounting for Derivative Instruments and Hedging Activities" as amended (hereinafter referred to as SFAS 133). Following SFAS 133, all derivatives are recognized on the Balance Sheet at their fair value and are classified as either assets or liabilities, depending on the nature (debit or credit) of their net fair value amount.

Changes in the fair value of investment derivatives and the related interest component are recorded in Income from investments. The interest component of lending and borrowing derivatives is recorded in loan income and borrowing expense, respectively, over the life of the derivative contract.

The Bank occasionally issues debt securities that contain an embedded derivative. The Bank assesses whether the economic characteristics of the embedded derivative are clearly and closely related to the economic characteristics of the debt security, excluding the embedded derivative features, that is, the host contract. Debt securities that contain an embedded derivative that possesses economic characteristics that are not clearly and closely related to the economic characteristics of the host contract, and would separately meet the definition of a derivative, are carried at fair value, as allowed by SFAS 155.

Administrative expenses
Substantially all administrative expenses of the Bank, including depreciation, are allocated between the Ordinary Capital and the FSO, pursuant to an allocation method approved by the Board of Executive Directors. Following this allocation method, during 2006, the effective ratio of administrative expenses charged to the Ordinary Capital was 81.3% and 18.7% to the FSO (2005—81.5% and 18.5%; 2004—84.4% and 15.6%).

Special programs
Special programs provide financing for non-reimbursable and contingent recovery assistance to borrowing member countries. The individual projects under these programs are recorded as Special programs expense at the time of approval. Cancellations of undisbursed balances and recuperations of contingent recovery financings are recognized as an offset to Special programs expense in the period in which they occur.

Taxes
The Bank, its property, other assets, income and the operations and transactions it carries out pursuant to the Agreement are immune from all taxation and from all customs duties in its member countries.

Note C – Restricted Currencies
At December 31, 2006, Cash includes $142 million (2005—$137 million) in currencies of regional borrowing members. These amounts may be used by the Bank in Ordinary Capital lending operations and for administrative expenses. The amount of $26 million (2005—$24 million) has been restricted by one member, in accordance with the provisions of the Agreement, to be used for making payments for goods and services produced in its territory.

Note D – Investments
As part of its overall portfolio management strategy, the Bank invests in government, agency, corporate, and bank obligations, asset-backed and mortgage-backed securities, and related financial derivative instruments, primarily currency and interest rate swaps.

For government and agency obligations, including securities issued by an instrumentality of a government or any other official entity, the Bank's policy is to invest in obligations issued or unconditionally guaranteed by governments of certain countries with a minimum credit quality equivalent to a AA– rating (agency asset-backed and mortgage-backed securities require a

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credit quality equivalent to a AAA rating). Obligations issued by multilateral organizations require a credit quality equivalent to a AAA rating. In addition, the Bank invests in bank obligations issued or guaranteed by an entity with a senior debt securities rating of at least A+, and in corporate, asset-backed, and mortgage-backed securities with credit quality equivalent to a AAA rating. The Bank also invests in short-term securities of the eligible investment asset classes mentioned above, provided that they carry only the highest short-term credit ratings.

A summary of the trading portfolio instruments at December 31, 2006 and 2005 is shown in the Summary Statement of Trading Investments and Swaps in Appendix I-1. In addition, a summary of the held-to-maturity portfolio and the portfolio's maturity structure at December 31, 2006 and 2005 are shown in the Summary Statement of Held-to-Maturity Investments in Appendix I-2.

Net unrealized gains (losses) on trading portfolio instruments held at December 31, 2006, of $3 million (2005—$(3) million; 2004—$(1) million) were included in Income from investments.

As of December 31, 2006, the Bank does not have any investment that is other-than-temporarily impaired. Held-to-maturity investments with continuous unrealized losses, that are not deemed to be other-than-temporarily impaired as of December 31, 2006 and 2005, are summarized below (in millions):

	December 31, 2006					
	Less than 12 Months		12 Months or Greater		Total	
Category of Investments	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of other governments and agencies[1]	$942	$(9)	$905	$(19)	$1,847	$(28)
Asset-backed and mortgage-backed securities	—	—	77	(2)	77	(2)
Total	$942	$(9)	$982	$(21)	$1,924	$(30)

	December 31, 2005					
	Less than 12 Months		12 Months or Greater		Total	
Category of Investments	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of other governments and agencies[1]	$853	$(8)	$174	$(6)	$1,027	$(14)
Asset-backed and mortgage-backed securities	—	—	39	(1)	39	(1)
Total	$853	$(8)	$213	$(7)	$1,066	$(15)

[1] Comprises non-U.S. governments and agencies.

The Bank only invests in high credit quality instruments. At December 31, 2006, 68% of the Held-to-maturity investments are rated AAA, 18% AA and 14% A. The unrealized losses on all categories of investments were caused by interest rate increases and are not related to a deterioration in credit quality. Because the Bank has the ability and intent to hold these investments until maturity, it does not consider these investments to be other-than-temporarily impaired at December 31, 2006, that is, the Bank expects to collect all amounts due according to the contractual terms prevailing on the acquisition date of these investments.

Note E – Loans and Guarantees Outstanding

Approved loans are disbursed to borrowers in accordance with the requirements of the project being financed; however, disbursements do not begin until the borrower and guarantor, if any, fulfill certain conditions precedent as required by contract.

The loan portfolio includes sovereign-guaranteed i) single currency pool loans (Single Currency Facility (SCF) and U.S. Dollar Window Program) as well as multicurrency pool loans (CPS loans), and ii) single currency non-pool loans (Emergency Lending Facility). In addition, the loan portfolio includes non-sovereign-guaranteed loans.

SCF loans are denominated in one of four currencies: United States dollars, euro, Japanese yen and Swiss francs, or in a combination of such currencies, with LIBOR-based or adjustable interest rates, both at the option of the borrower. The interest rate on SCF loans for which a LIBOR–based pricing alternative is not selected resets semi-annually, based on the effective cost during the previous six months of each of the single-currency pools of borrowings allocated to fund such loans, plus the Bank's spread. The interest rate on LIBOR–based SCF loans resets quarterly, based on the currency-specific three-month LIBOR plus a pool-based margin reflecting the Bank's sub-LIBOR funding cost and the risk mitigation cost, and the Bank's spread.

The Bank maintains a targeted currency composition in its CPS of 50% United States dollars, 25% Japanese yen and 25% European currencies. The interest rate on CPS loans made from January 1, 1983 to December 31, 1989 is fixed. The interest rate on CPS loans made after that date is adjusted twice a year based on the effective cost during the previous six months of a pool of borrowings allocated to fund such loans, plus the Bank's spread. Since September 2003, CPS loans are no longer available to borrowers.

Under the Emergency Lending Facility, funding is provided to address financial emergencies in the region for a revolving aggregate amount of up to $6 billion. Loans are denominated in United States dollars, have a term not to exceed five years, and principal repayments begin after three years. These loans carry a six-month LIBOR interest rate plus a spread of 400 basis points.

Non-sovereign-guaranteed loans are denominated in United States dollars and borrowers have the option of either a LIBOR-based fixed or floating-rate loan. The interest rate on fixed-rate loans is based on a LIBOR funding cost plus a credit spread. For floating-rate loans, the interest rate resets every one, three or six months based on a LIBOR rate plus a credit spread. The credit spreads and fees on these loans are set on a case-by-case basis.

Under the Local Currency Facility approved in 2005, borrowers have the option to receive local currency financing under three different modalities: i) local currency conversion of future loan disbursements and/or outstanding loan balances; ii) direct swaps into local currency against existing Bank debt; and iii) local currency conversion of called guarantees. The use of these modalities is subject to the availability of the respective local currency and the appropriate risk mitigation instrument(s) in the financial markets. As of December 31, 2006, the Bank has carried out cumulative local currency conversions of loan disbursements amounting to $76 million (2005—$19 million).

A summary statement of loans outstanding by country is presented in Appendix I-3 and a summary of the outstanding loans by currency and product type and their maturity structure at December 31, 2006 and 2005 is shown in Appendix I-4.

Inter-American Investment Corporation (IIC)
The Bank has approved a loan to the IIC (a separate international organization whose 43 member countries are also members of the Bank) of $300 million. Disbursements under this loan are to be made in United States dollars and carry a LIBOR-based interest rate. There were no amounts outstanding as of December 31, 2006 and 2005.

Loan participations and guarantees
Under the loan contracts with its borrowers, the Bank has the right to sell loan participations to commercial banks or other financial institutions, while reserving to itself the administration of the loans. As of December 31, 2006, there were $1,205 million (2005—$1,628 million) in outstanding participations in non-sovereign-guaranteed loans not included in the Balance Sheet.

As of December 31, 2006, the Bank had approved, net of cancellations and expirations, non-trade-finance guarantees without sovereign counter-guarantees in the amount of $512 million (2005—$360 million). In addition, during 2006 the Bank approved its first guarantee with sovereign counter-guarantee in the amount of $60 million. The Bank also has a Trade Finance Facilitation Program to provide partial credit guarantees without sovereign counter-guarantees on trade-finance transactions. This Program, which began to operate in July 2005, authorizes up to $40 million in credit support per approved trade-finance bank, and an aggregate of no more than $400 million outstanding at any time. As of December 31, 2006, trade-finance guarantee lines of credit in the amount of $423 million had been authorized (2005—$270 million) under this Program.

As of December 31, 2006, guarantees of $379 million (2005—$319 million) were outstanding and subject to call. An amount of $61 million (2005—$72 million) has been re-insured to reduce the Bank's exposure. Outstanding guarantees have remaining maturities ranging from 4 to 19 years, except for trade related guarantees that have maturities of up to three years. As of December 31, 2006, no guarantees provided by the Bank had been called.

IFF subsidy
The IFF was established in 1983 by the Board of Governors of the Bank to subsidize part of the interest payments for which certain borrowers are liable on loans from the resources of the Ordinary Capital. Up to December 31, 2005, the IFF subsidized 100% of certain principal and interest payments on Ordinary Capital loans, under the Enhanced Heavily Indebted Poor Countries (HIPC) Initiative, which is a concerted international initiative for addressing the debt problems of a group of countries identified as heavily indebted poor countries in which the Bank participates. During 2006, the IFF paid $43 million (2005—$43 million; 2004—$50 million) of interest and no principal (2005—$0 million; 2004—$8 million) on behalf of the borrowers. The IFF is funded primarily from the general reserve of the FSO.

Nonaccrual and impaired loans and allowance for loan and guarantee losses
At December 31, 2006, all loans were performing except for certain non-sovereign-guaranteed loans, which were classified as impaired and were in nonaccrual status. The recorded investment in impaired loans at December 31, 2006 was $66 million (2005—$196 million). The average recorded investment in impaired loans during 2006 was $117 million (2005—$216 million). During 2006, income recognized on loans while impaired was $13 million (2005—$42 million, including $29 million related to prior years; 2004—$12 million). If these loans had not been impaired, income recognized would have been $11 million (2005—$16 million; 2004—$18 million). All impaired loans have specific allowances for loan losses amounting to $19 million at December 31, 2006 (2005—$105 million).

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NOTES TO FINANCIAL STATEMENTS (continued)

The changes in the allowance for loan and guarantee losses for the years ended December 31, 2006 and 2005 were as follows (in millions):

	2006	2005
Balance, beginning of year	$188	$199
Credit for loan and guarantee losses	(48)	(14)
Non-sovereign-guaranteed loans:		
Write-offs	(42)	(6)
Recoveries	6	9
Balance, end of year	$104	$188
Composed of:		
Allowance for loan losses	$ 90	$175
Allowance for guarantee losses[1]	14	13
Total	$104	$188

[1] Included in Accounts payable and accrued expenses.

Note F – Property

As of December 31, 2006 and 2005, Property, net consists of the following (in millions):

	2006	2005
Land, buildings, improvements, capitalized software and equipment, at cost	$ 499	$ 484
Less: accumulated depreciation	(198)	(158)
	$ 301	$ 326

Note G – Borrowings

The objective of the Bank's borrowing policy is to secure long-term capital market access, volume, and cost effectiveness. Medium- and long-term borrowings at December 31, 2006 consist of loans, notes and bonds issued in various currencies at contracted interest rates ranging from 0.00% to 14.00%, before swaps, and from (0.02%) (equivalent to JPY-LIBOR less 58 basis points) to 12.25%, after swaps, with various maturity dates through 2027. A summary of the medium- and long-term borrowing portfolio and its maturity structure at December 31, 2006 and 2005 is shown in Appendix I-5.

The Bank has short-term borrowing facilities that consist of a discount notes program and uncommitted borrowing lines from various commercial banks. Discount notes are issued in amounts not less than $100,000, with maturities of up to 360 days.

Borrowing expenses have been reduced by net interest receipts from related borrowing swap transactions amounting to $307 million during 2006 (2005—$564 million; 2004—$869 million).

Note H – Derivatives and Hedging Activities

Risk management strategy and use of derivatives

The Bank's financial risk management strategy is designed to strengthen the Bank's ability to fulfill its purpose. This strategy consists primarily of designing, implementing, updating, and monitoring the Bank's interrelated set of financial policies and guidelines, and utilizing appropriate financial instruments and organizational structures. Financial derivative instruments are an important component of the set of financial instruments used by the Bank to enhance its financial efficiency while achieving its risk management objectives. These instruments, mostly currency and interest rate swaps, are used primarily for hedging purposes as part of the Bank's asset and liability management.

The majority of the current borrowing operations include swaps to hedge a specific underlying liability, producing the funding required (i.e., the appropriate currency and interest rate type). The Bank also uses interest rate swaps to hedge private sector fixed-rate loans and investment swaps that hedge a particular underlying investment security and produce the appropriate vehicle in which to invest existing cash. In addition, the Bank enters into interest rate caps to protect against sudden interest rate increases on floating rate borrowings funding its LIBOR-based SCF loans.

Effects of SFAS 133 and currency transaction adjustments

Following the requirements of SFAS 133, the Bank records all derivatives at fair value on the Balance Sheet, with changes in fair value reported in Effects of SFAS 133 and currency transaction adjustments on the Statement of Income and Retained Earnings.

On January 1, 2001, the Bank adopted SFAS 133 and designated substantially all its borrowing and lending currency and interest rate swaps in fair value hedging relationships under this standard. Gains or losses on borrowings and loans for which a fair value exposure was being hedged were recorded in income and were offset by the fair value adjustment of the related derivative instrument. Upon discontinuance of hedge accounting on January 1, 2004, the Bank began to amortize the fair value adjustments on the borrowings and loans over the remaining lives of the related bonds or loans. This amortization is included in Effects of SFAS 133 and currency transaction adjustments.

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NOTES TO FINANCIAL STATEMENTS (continued)

Effects of SFAS 133 and currency transaction adjustments for the years ended December 31, 2006, 2005 and 2004 comprise the following (in millions):

	2006	2005	2004
Increase (decrease) in fair value of derivative instruments due to movements in:			
Exchange rates	$ 619	$(568)	$ 630
Interest rates	(469)	5	48
Total change in fair value of derivatives	150	(563)	678
Currency transaction (losses) gains on borrowings	(589)	536	(603)
Change in fair value of hybrid borrowings	1	—	—
Amortization of borrowing and loan fair values adjustments	62	85	250
Reclassification to income—cash flow hedges	(8)	(8)	(11)
Total	$(384)	$ 50	$ 314

The Bank's borrowings in non-functional currencies are fully swapped to functional currencies, thus protecting the Bank against fluctuations in exchange rates. During 2006, positive exchange rate changes, affecting the value of the borrowing swaps, amounting to $619 million (2005—negative changes of $568 million; 2004—positive changes of $630 million) offset currency transaction losses on borrowings of $589 million (2005—gains of $536 million; 2004—losses of $603 million).

Note I – Commercial Credit Risk

Commercial credit risk is the exposure to losses that could result from either the default or the downgrade by a credit rating agency of one of the Bank's investment, trading or derivative counterparties. The main sources of commercial credit risk are the financial instruments in which the Bank invests its liquidity. The primary objective in the management of the liquid assets is the maintenance of a conservative exposure to credit, market and liquidity risks. Consequently, the Bank invests only in high quality debt instruments issued by sovereigns, agencies, banks and corporate entities. In addition, the Bank limits its capital market activities to authorized counterparties, issuers and dealers selected on the basis of conservative risk management policies, and establishes exposure and term limits for those counterparties, issuers and dealers based on their size and creditworthiness.

As part of its regular investment, funding and asset and liability management activities, the Bank uses derivative instruments, mostly currency and interest rate swaps, primarily for hedging purposes. The Bank has established exposure limits for each derivative counterparty and has entered into master derivative agreements that contain enforceable close-out netting provisions. These master agreements also provide for collateralization in the event that the mark-to-market exposure exceeds certain contractual limits. The Bank does not expect nonperformance by any of its counterparties. As of December 31, 2006, the Bank had received collateral of $1,264 million (2005—$885 million) as required under its master derivative agreements.

The derivative credit exposures shown below represent the maximum potential loss, based on the gross fair value of the financial instruments without consideration of close-out netting provisions on master derivative agreements, the Bank would incur if the parties to the derivative financial instruments failed completely to perform according to the terms of the contracts and the collateral or other security, if any, for the amount due proved to be of no value. As of December 31, 2006 and 2005, such credit exposures, prior to consideration of any master derivative agreements or posted collateral, were as follows (in millions):

	2006	2005
Investments—Trading Portfolio		
Currency swaps	$ —	$ 3
Interest rate swaps	8	4
Borrowing Portfolio		
Currency swaps	1,797	1,459
Interest rate swaps	113	190
Loan Portfolio		
Interest rate swaps	5	4

Note J – Capital Stock and Voting Power

Capital stock

Capital stock consists of "paid-in" and "callable" shares. The subscribed "paid-in" capital stock has been paid in gold and/or United States dollars and in the currency of the respective member, which in some cases has been made freely convertible, in accordance with the terms for the respective increase in capital. Non-negotiable, non-interest-bearing demand obligations have been accepted in lieu of the immediate payment of all or any part of the member's subscribed "paid-in" capital stock. The subscribed "callable" portion of capital may only be called when required to meet obligations of the Bank created by borrowings of funds for inclusion in the Ordinary Capital resources or guarantees chargeable to such resources and is payable at the option of the member either in gold, in United States dollars, in the currency of the member country, or in the currency required to discharge the obligations of the Bank for the purpose for which the call is made. For a Statement of Subscriptions to Capital Stock at December 31, 2006 and 2005, see Appendix I-6.

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NOTES TO FINANCIAL STATEMENTS (continued)

The composition of the net receivable from members as of December 31, 2006 and 2005 is as follows (in millions):

	2006	2005
Regional developing members	$ 406	$ 419
Canada	(93)	(95)
Non-regional members	(210)	(69)
Total	$ 103	$ 255

These amounts are represented on the Balance Sheet as follows (in millions):

	2006	2005
Receivable from members	$ 418	$ 443
Amounts payable to maintain value of currency holdings	(315)	(188)
Total	$ 103	$ 255

Voting power

Under the Agreement, each member country shall have 135 votes plus one vote for each share of the Bank held by that country. The Agreement, as amended by the Eighth General Increase in the Resources of the Inter-American Development Bank, also provides that no increase in the capital stock subscription of any member shall have the effect of reducing the voting power of the regional developing members below 50.005%, of the United States below 30%, and of Canada below 4% of the total voting power, leaving the remaining voting power available for nonregional members at a maximum of 15.995%, including approximately 5% for Japan.

Total capital stock subscriptions and the voting power of the member countries as of December 31, 2006 are shown in the Statement of Subscriptions to Capital Stock and Voting Power in Appendix I-7.

Note K – Retained Earnings

The composition of Retained earnings as of December 31, 2006 and 2005 is as follows (in millions):

	2006	2005
General reserve	$11,777	$11,534
Special reserve	2,665	2,665
Total	$14,442	$14,199

In each of the years 2001 through 2004, the Bank made transfers of $27.2 million from the net income of the Ordinary Capital to the FSO. Each of these transfers represented one fifth of unallocated special contributions to the FSO provided for in the agreement for the Eighth General Increase in the Resources of the Inter-American Development Bank. Net income transfers reduce the general reserve of the Bank.

Note L – Accumulated Other Comprehensive Income

Other comprehensive income comprises the effects of SFAS 133 and SFAS 158 and currency translation adjustments. These items, except SFAS 158 adopted as of December 31, 2006, are presented on the Statement of Comprehensive Income.

The following is a summary of changes in Accumulated other comprehensive income for the years ended December 31, 2006 and 2005 (in millions):

	Translation Adjustments Allocation				
	General Reserve	Special Reserve	SFAS 133 Adjustments	SFAS 158 Adjustments	Total
Balance at January 1, 2005	$ 879	$(130)	$(15)	$ —	$ 734
Translation adjustments	(484)	(70)	—	—	(554)
Reclassification to income—cash flow hedges	—	—	8	—	8
Balance at December 31, 2005	395	(200)	(7)	—	188
Translation adjustments	117	32	—	—	149
Reclassification to income—cash flow hedges	—	—	8	—	8
Initial recognition of deferred (cost) credit for postretirement benefits:					
Net actuarial gain	—	—	—	698	698
Prior service cost	—	—	—	(17)	(17)
Balance at December 31, 2006	$ 512	$(168)	$ 1	$681	$1,026

Note M – Pension and Postretirement Benefit Plans

The Bank has two defined benefit retirement plans (Plans), the Staff Retirement Plan (SRP) for the pension benefit of its international employees and the employees of the IIC, and the Local Retirement Plan (LRP) for the pension benefit of national employees in the country offices. The Plans are funded by employee and Bank contributions in accordance with the provisions of the Plans. Any and all Bank contributions to the Plans are irrevocable and are held separately in retirement funds solely for the payment of benefits under the Plans.

The Bank also provides certain health care and other benefits to retirees. All current staff of the Bank and the IIC who contribute to the SRP and LRP while in active service and who meet certain requirements are eligible for postretirement benefits under the Postretirement Benefits Plan (PRBP). Retirees contribute toward the Bank's health care program based on an established premium schedule. The Bank contributes the remainder of the actuarially determined cost of future health and other benefits. While all contributions and all other assets and income of the PRBP remain the property of the Bank, they are held and administered separately and apart from the other

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NOTES TO FINANCIAL STATEMENTS (continued)

property and assets of the Bank solely for the purpose of payment of benefits under the PRBP.

Since both the Bank and the IIC participate in the SRP and the PRBP, each employer presents its respective share of these plans. The amounts presented below reflect the Bank's proportionate share of costs, assets and obligations of the Plans and the PRBP.

Obligations and funded status

The Bank uses a December 31 measurement date for the Plans and the PRBP. The following table summarizes the Bank's share of the change in benefit obligation, change in plan assets, and funded status of the Plans and the PRBP, and the amounts recognized on the Balance Sheet for the years ended December 31, 2006, 2005 and 2004 (in millions):

	Pension Benefits			Postretirement Benefits		
	2006	2005	2004	2006	2005	2004
Change in benefit obligation						
Benefit obligation, beginning of year	$2,046	$1,794	$1,671	$ 810	$733	$703
Service cost	58	56	47	31	28	22
Interest cost	112	105	96	44	42	39
Plan participants' contributions	21	20	18	—	—	—
Actuarial loss (gain)	39	136	10	21	23	(18)
Plan amendments	—	—	7	—	—	1
Benefits paid	(69)	(65)	(55)	(20)	(16)	(14)
Benefit obligation, end of year	2,207	2,046	1,794	886	810	733
Change in plan assets						
Fair value of plan assets, beginning of year	2,499	2,259	2,015	994	899	811
Actual return on plan assets	339	255	253	140	99	95
Employer contribution	35	30	28	16	12	7
Plan participants' contributions	21	20	18	—	—	—
Benefits paid	(69)	(65)	(55)	(20)	(16)	(14)
Net payments from other plans	1	—	—	—	—	—
Fair value of plan assets, end of year	2,826	2,499	2,259	1,130	994	899
Funded status, end of year	619	453	465	244	184	166
Unrecognized:						
Net actuarial gain	—	(331)	(344)	—	(142)	(118)
Prior service cost	—	13	15	—	9	10
Net amount recognized	$ 619	$ 135	$ 136	$ 244	$ 51	$ 58
Amounts recognized on the Balance Sheet consist of:						
Postretirement benefit assets	$ 619	$ —	$ —	$ 244	$ —	$ —
Prepaid benefit cost	—	136	136	—	51	58
Accrued benefit liability	—	(1)	—	—	—	—
Net amount recognized	$ 619	$ 135	$ 136	$ 244	$ 51	$ 58
Amounts recognized in Accumulated other comprehensive income consist of:						
Net actuarial gain	$ (492)			$ (206)		
Prior service cost	10			7		
Net amount recognized	$ (482)			$ (199)		

The incremental effect of applying SFAS 158 on individual line items on the Balance Sheet as of December 31, 2006 is as follows (in millions):

	Before Application of SFAS 158	Adjustments	After Application of SFAS 158
Postretirement benefit assets	$ 182	$681	$ 863
Other assets	836	681	1,517
Total assets	**65,794**	**681**	**66,475**
Accumulated other comprehensive income	345	681	1,026
Total equity	**19,127**	**681**	**19,808**
Total liabilities and equity	**65,794**	**681**	**66,475**

The accumulated benefit obligation for the Plans was $1,911 million and $1,765 million at December 31, 2006 and 2005, respectively.

Components of net periodic benefit cost

Net periodic benefit cost for the years ended December 31, 2006, 2005 and 2004 consists of the following components (in millions):

	Pension Benefits			Postretirement Benefits		
	2006	2005	2004	2006	2005	2004
Service cost	$ 58	$ 56	$ 47	$ 31	$ 28	$ 22
Interest cost	112	105	96	44	42	39
Expected return on plan assets	(139)	(132)	(128)	(55)	(53)	(53)
Amortization of:						
Prior service cost	2	2	1	2	2	—
Unrecognized net actuarial gain	—	—	—	—	—	(2)
Net periodic benefit cost	$ 33	$ 31	$ 16	$ 22	$ 19	$ 6
Of which:						
Ordinary Capital's share	$ 26	$ 25	$ 13	$ 17	$ 15	$ 5
FSO's share	7	6	3	5	4	1

The Bank allocates the net periodic benefit cost between the Ordinary Capital and the FSO in accordance with the allocation method approved by the Board of Executive Directors for administrative expenses. Benefit cost is included in Administrative expenses.

The estimated prior service cost that will be amortized from Accumulated other comprehensive income into net periodic benefit cost during 2007 is $2 million for the Plans and $2 million for the PRBP.

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NOTES TO FINANCIAL STATEMENTS (continued)

Actuarial assumptions

The actuarial assumptions used are based on financial market interest rates, past experience, and management's best estimate of future benefit changes and economic conditions. Changes in these assumptions will impact future benefit costs and obligations. Actuarial gains and losses occur when actual results are different from expected results. Unrecognized actuarial gains and losses which exceed 10% of the greater of the benefit obligation or market-related value of plan assets at the beginning of the period are amortized over the average remaining service period of active employees expected to receive benefits under the SRP, LRP and PRBP, which approximates 10.8, 12.3 and 11.5 years, respectively.

Unrecognized prior service cost is amortized over 10.8 years for the SRP, 12.3 years for the LRP, and 7.5 years for the PRBP.

The weighted-average assumptions used to determine the benefit obligations and net periodic benefit cost were as follows:

Weighted-average assumptions used to determine benefit obligations at December 31,	Pension Benefits			Postretirement Benefits		
	2006	2005	2004	2006	2005	2004
Discount rate	6.00%	5.50%	5.50%	6.00%	5.50%	5.50%
Rate of salary increase SRP	6.00%	5.10%	5.10%			
Rate of salary increase LRP	7.80%	7.30%	6.90%			

Weighted-average assumptions used to determine net periodic benefit cost for the years ended December 31,	Pension Benefits			Postretirement Benefits		
	2006	2005	2004	2006	2005	2004
Discount rate	5.50%	5.50%	5.75%	5.50%	5.50%	5.75%
Expected long-term return on plan assets	6.75%	6.75%	6.75%	6.75%	6.75%	6.75%
Rate of salary increase SRP	5.10%	5.10%	5.30%			
Rate of salary increase LRP	7.30%	6.90%	7.20%			

The expected yearly rate of return on plan assets reflects the historical rate of returns of asset categories employed by the plans and conservatively applying those returns in formulating the investment policy asset allocations. The discount rates used in determining the benefit obligations are selected by reference to the year-end AAA and AA corporate bond rates.

For participants assumed to retire in the United States, the accumulated postretirement benefit obligation was determined using the following health care cost trend rates at December 31:

	2006	2005	2004
Health care cost trend rates assumed for next year:			
Medical	8.00%	8.00%	8.00%
Prescription drugs	9.00%	9.50%	11.00%
Dental	6.50%	6.50%	6.50%
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)	5.00%	4.50%	4.50%
Year that the rate reaches the ultimate trend rate	2013	2013	2013

For those participants assumed to retire outside of the United States, a 8.00% (2005—8.00%; 2004—8.00%) health care cost trend rate was used.

Assumed health care cost trend rates have a significant effect on the amounts reported for the PRBP. A one-percentage point change in assumed health care cost trend rates would have the following effects as of December 31, 2006 (in millions):

	1-Percentage Point Increase	1-Percentage Point Decrease
Effect on total of service and interest cost components	$ 13	$(10)
Effect on postretirement benefit obligation	105	(83)

Plan assets

The Plans and PRBP weighted-average asset allocations at December 31, 2006 and 2005, by asset category, are as follows:

	Plans		PRBP	
Asset category	2006	2005	2006	2005
U.S. equities	35%	35%	40%	39%
Non-U.S. equities	26%	31%	31%	35%
Emerging market equities	3%	—	—	—
Emerging market debt	2%	—	—	—
Fixed income bonds and funds	20%	20%	19%	17%
U.S. inflation-indexed bonds	6%	5%	9%	8%
Real estate investment funds and equities	6%	6%	—	—
Commodity index futures	2%	3%	—	—
Other	—	—	1%	1%
Total	100%	100%	100%	100%

ORDINARY CAPITAL
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NOTES TO FINANCIAL STATEMENTS (continued)

The assets of the Plans and the PRBP are managed primarily by investment managers employed by the Bank who are provided with investment guidelines that take into account the Plans and PRBP investment policies. Investment policies have been developed so that, consistent with historical returns, there is a high equity allocation with the expectation of sufficient returns to meet long-term funding needs.

Investments maintain an average exposure between 60% and 65% to a well-diversified pool of equities. Assets are also invested in fixed-income securities (20%) to protect against disinflation, a mix of other types of investments (10% to 15%) that are expected to react positively to rising inflation to provide protection against loss of purchasing power, emerging market equities (0% to 5%), and emerging market debt (0% to 5%). The investment policy target allocations as of December 31, 2006 are as follows:

	SRP	LRP	PRBP
U.S. equities	35%	40%	40%
Non-U.S. equities	25%	30%	30%
Emerging market securities[(1)]	5%	—	—
Fixed income	20%	20%	20%
Inflation-Sensitive investments[(2)]	15%	10%	10%

(1) Comprised of emerging market equities and debt.
(2) Comprised of inflation-indexed U.S. Government bonds (5% to 15%), real estate investment funds and equities (0% to 6%), and full-collateralized commodity index futures (0% to 4%) for the SRP, inflation-indexed U.S. Government bonds (5% to 10%) and real estate investment funds and equities (0% to 5%) for the LRP, and inflation-indexed U.S. Government bonds (10%) for the PRBP.

Risk management is achieved by the continuous monitoring of each asset category level and investment manager. The investments are rebalanced toward the policy target allocations to the extent possible from cash flows. If cash flows are insufficient to maintain target weights, transfers among the managers' accounts are made at least annually. Investment managers generally are not allowed to invest more than 5% of their respective portfolios in the securities of a single issuer other than the U.S. Government. The use of derivatives by an investment manager must be specifically approved for each instrument.

Cash flows

Contributions

Contributions from the Bank to the Plans and the PRBP during 2007 are expected to be approximately $37 million and $16 million, respectively. All contributions are made in cash.

Estimated future benefit payments

The following table shows the benefit payments, which reflect expected future service, as appropriate, expected to be paid in each of the next five years and in the aggregate for the subsequent five years (in millions). These amounts are based on the same assumptions used to measure the benefit obligation at December 31, 2006.

Year	Plans	PRBP
2007	$ 77	$ 25
2008	82	27
2009	88	30
2010	94	32
2011	100	35
2012–2016	587	211

Note N – Reconciliation of Net Income to Net Cash (Used In) Provided by Operating Activities

A reconciliation of Net income to Net cash (used in) provided by operating activities, as shown on the Statement of Cash Flows, is as follows (in millions):

	Years ended December 31,		
	2006	2005	2004
Net income	$ 243	$ 762	$1,176
Difference between amounts accrued and amounts paid or collected for:			
Loan income	(9)	(8)	(72)
Investment income	(19)	(7)	(1)
Net unrealized gain on trading investments	(12)	(1)	(14)
Interest and other costs of borrowings, after swaps	213	188	124
Administrative expenses, including depreciation	48	53	(10)
Special programs	27	11	—
Effects of SFAS 133 and currency transaction adjustments	384	(50)	(279)
Net (increase) decrease in trading investments	(1,796)	(1,341)	2,076
(Credit) provision for loan and guarantee losses	(48)	(14)	21
Net cash (used in) provided by operating activities	$ (969)	$ (407)	$3,021
Supplemental disclosure of noncash activities			
Increase (decrease) resulting from exchange rate fluctuations:			
Trading investments	$ 316	$ (272)	$ 170
Held-to-maturity investments	167	(271)	194
Loans outstanding	366	(1,377)	624
Borrowings	536	(1,229)	665
Receivable from members-net	(139)	187	(164)

ORDINARY CAPITAL
INTER-AMERICAN DEVELOPMENT BANK

NOTES TO FINANCIAL STATEMENTS (continued)

Note O – Segment Reporting

Management has determined that the Bank has only one reportable segment since it does not manage its operations by allocating resources based on a determination of the contributions to net income of individual operations. The Bank does not differentiate between the nature of the products or services provided, the preparation process, or the method for providing the services among individual countries. For the years 2006, 2005 and 2004, loans made to or guaranteed by three countries individually generated in excess of 10 percent of loan income, as follows (in millions):

	Years ended December 31,		
	2006	2005	2004
Brazil	$540	$478	$551
Argentina	476	460	440
Mexico	330	333	345

Note P – Fair Values of Financial Instruments

The following methods and assumptions were used by the Bank in estimating the fair value for its financial instruments:

Cash: The carrying amount reported in the Balance Sheet for cash approximates fair value.

Investments: Fair values for investment securities are based on quoted market prices, where available; otherwise they are based on dealer prices of comparable instruments or discounted cash flows.

Loans: The Bank is one of very few lenders of development loans to Latin American and Caribbean countries. There is no secondary market for development loans. For all loans and related commitments, the Bank is of the opinion that, due to its unique position in lending operations and the absence of a secondary market, it is not practicable to estimate a fair value for its lending portfolio.

Swaps: Fair values for interest rate and currency swaps are based on pricing models and represent the estimated cost of replacing these contracts.

Borrowings: The fair values of borrowings are based on quoted market prices, where available; otherwise they are based on dealer prices of comparable instruments or discounted cash flows.

The following table presents the Bank's estimates of fair value for its financial instruments, along with the respective carrying amounts, as of December 31, 2006 and 2005 (in millions):

	2006		2005	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Cash	$ 276	$ 276	$ 223	$ 223
Investments				
Trading	12,278	12,278	10,183	10,183
Held-to-maturity	3,543	3,516	3,414	3,414
Loans outstanding, net	45,842	N/A	47,960	N/A
Currency and interest rate swaps receivable				
Investments—trading	2	2	3	3
Loans	5	5	5	5
Borrowings	1,880	1,880	1,596	1,596
Borrowings				
Short-term	658	658	926	926
Medium- and long-term	44,030	44,080	44,167	44,918
Currency and interest rate swaps payable				
Investments—trading	1	1	61	61
Loans	9	9	10	10
Borrowings	742	742	491	491

N/A = Not available

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APPENDIX I-1

SUMMARY STATEMENT OF TRADING INVESTMENTS AND SWAPS – NOTE D

December 31, 2006
Expressed in millions of United States dollars

	Euro	United States dollars	All currencies
Obligations of the United States Government and its corporations and agencies:			
Carrying value	—	523	523[1]
Average balance during year	15	216	231
Net gains (losses) for the year	(1)	1	—
Obligations of other governments and agencies:			
Carrying value	—	—	—
Average balance during year	112	50	162
Net losses for the year	(7)	(1)	(8)
Bank obligations:			
Carrying value	954	2,232	3,186
Average balance during year	1,043	2,176	3,219
Net gains for the year	—	1	1
Corporate securities:			
Carrying value	—	481	481
Average balance during year	51	389	440
Net gains (losses) for the year	—	—	—
Asset-backed and mortgage-backed securities:			
Carrying value	2,351	5,737	8,088
Average balance during year	2,164	4,934	7,098
Net gains for the year	2	45	47
Total trading investments:			
Carrying value	3,305	8,973	12,278
Average balance during year	3,385	7,765	11,150
Net gains (losses) for the year	(6)	46	40
Currency swaps receivable:			
Carrying value[2]	—	—	—
Average balance during year	—	100	100
Net gains (losses) for the year	—	—	—
Currency swaps payable:			
Carrying value[2]	—	—	—
Average balance during year	(120)	—	(120)
Net gains for the year	6	—	6
Net interest rate swaps:			
Carrying value[2]	—	1	1
Average balance during year	—	—	—
Net gains for the year	4	—	4
Total trading investments and swaps:			
Carrying value	3,305	8,974	12,279
Average balance during year	3,265	7,865	11,130
Net gains for the year	4	46	50
Return for the year (%)	3.15	5.37	4.73

(1) Includes obligations issued or guaranteed by Government-Sponsored Enterprises (GSE), such as debt and mortgage- and asset-backed securities, in the amount of $348 million. GSE obligations are not backed by the full faith and credit of the United States government.

(2) Carrying value of currency swaps represents the fair value of each individual receivable or (payable) leg, classified by their currency. Currency and interest rate swap agreements are stated in the Balance Sheet as assets or liabilities, depending on the nature (debit or credit) of the net fair value amount of these agreements.

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APPENDIX I-1

SUMMARY STATEMENT OF TRADING INVESTMENTS AND SWAPS – NOTE D

December 31, 2005
Expressed in millions of United States dollars

	Euro	United States dollars	All currencies
Obligations of the United States Government and its corporations and agencies:			
Carrying value	132	196	328[1]
Average balance during year	140	183	323
Net gains (losses) for the year	(4)	1	(3)
Obligations of other governments and agencies:			
Carrying value	256	99	355
Average balance during year	225	181	406
Net losses for the year	(3)	(7)	(10)
Bank obligations:			
Carrying value	415	1,845	2,260
Average balance during year	499	2,052	2,551
Net gains for the year	—	2	2
Corporate securities:			
Carrying value	161	323	484
Average balance during year	160	198	358
Net gains (losses) for the year	—	—	—
Asset-backed and mortgage-backed securities:			
Carrying value	2,082	4,674	6,756
Average balance during year	1,476	4,042	5,518
Net gains for the year	1	27	28
Total trading investments:			
Carrying value	3,046	7,137	10,183
Average balance during year	2,500	6,656	9,156
Net gains (losses) for the year	(6)	23	17
Currency swaps receivable:			
Carrying value[2]	—	251	251
Average balance during year	—	215	215
Net gains (losses) for the year	—	—	—
Currency swaps payable:			
Carrying value[2]	(304)	—	(304)
Average balance during year	(278)	—	(278)
Net gains for the year	4	—	4
Net interest rate swaps:			
Carrying value[2]	(3)	(2)	(5)
Average balance during year	(4)	(4)	(8)
Net gains for the year	1	7	8
Total trading investments and swaps:			
Carrying value	2,739	7,386	10,125
Average balance during year	2,218	6,867	9,085
Net gains (losses) for the year	(1)	30	29
Return for the year (%)	2.38	3.53	3.27

(1) Includes obligations issued or guaranteed by Government-Sponsored Enterprises (GSE), such as debt and mortgage- and asset-backed securities, in the amount of $328 million. GSE obligations are not backed by the full faith and credit of the United States government.

(2) Carrying value of currency swaps represents the fair value of each individual receivable or (payable) leg, classified by their currency. Currency and interest rate swap agreements are stated in the Balance Sheet as assets or liabilities, depending on the nature (debit or credit) of the net fair value amount of these agreements.

ORDINARY CAPITAL
INTER-AMERICAN DEVELOPMENT BANK

APPENDIX I-2

SUMMARY STATEMENT OF HELD-TO-MATURITY INVESTMENTS – NOTE D

December 31, 2006
Expressed in millions of United States dollars

	Euro	Japanese yen	Swiss francs	United States dollars	Other currencies	All currencies
Obligations of the United States Government and its corporations and agencies:						
Net carrying amount	66	—	—	5	—	71[1]
Gross unrealized gains	—	—	—	—	—	—
Gross unrealized losses	—	—	—	—	—	—
Fair value	66	—	—	5	—	71
Obligations of other governments and agencies:						
Net carrying amount	867	348	72	351	884	2,522
Gross unrealized gains	—	—	—	—	2	2
Gross unrealized losses	13	1	—	8	6	28
Fair value	854	347	72	343	880	2,496
Bank obligations:						
Net carrying amount	310	111	142	—	185	748
Gross unrealized gains	—	—	—	—	—	—
Gross unrealized losses	—	—	—	—	—	—
Fair value	310	111	142	—	185	748
Asset-backed and mortgage-backed securities:						
Net carrying amount	—	1	—	75	126	202
Gross unrealized gains	—	—	—	—	1	1
Gross unrealized losses	—	—	—	1	1	2
Fair value	—	1	—	74	126	201
Total held-to-maturity investments:						
Net carrying amount	1,243	460	214	431	1,195[2]	3,543
Gross unrealized gains	—	—	—	—	3	3
Gross unrealized losses	13	1	—	9	7	30
Fair value	1,230	459	214	422	1,191	3,516
Return for the year (%)	3.42	0.26	1.84	4.14	4.32	3.31

[1] Includes obligations issued or guaranteed by Government-Sponsored Enterprises (GSE), such as debt and mortgage- and asset-backed securities, in the amount of $71 million. GSE obligations are not backed by the full faith and credit of the United States government.

[2] The net carrying amount of held-to-maturity investments held in other currencies consists of the following:

Canadian dollars	$ 887
British pounds sterling	217
Other	91
Total	$1,195

MATURITY STRUCTURE OF HELD-TO-MATURITY INVESTMENTS

December 31, 2006
Expressed in millions of United States dollars

Year of maturity	Net carrying amount	Fair value
2007	$1,358	$1,358
2008 to 2011	2,182	2,156
2012	3	2
Total	$3,543	$3,516

ORDINARY CAPITAL
INTER-AMERICAN DEVELOPMENT BANK

APPENDIX I-2

SUMMARY STATEMENT OF HELD-TO-MATURITY INVESTMENTS – NOTE D

December 31, 2005
Expressed in millions of United States dollars

	Euro	Japanese yen	Swiss francs	United States dollars	Other currencies	All currencies
Obligations of the United States Government and its corporations and agencies:						
Net carrying amount	114	—	—	5	—	119[1]
Gross unrealized gains	1	—	—	—	—	1
Gross unrealized losses	—	—	—	—	—	—
Fair value	115	—	—	5	—	120
Obligations of other governments and agencies:						
Net carrying amount	628	331	91	411	759	2,220
Gross unrealized gains	5	—	1	—	5	11
Gross unrealized losses	2	—	—	9	3	14
Fair value	631	331	92	402	761	2,217
Bank obligations:						
Net carrying amount	299	95	50	103	191	738
Gross unrealized gains	1	—	—	—	—	1
Gross unrealized losses	—	—	—	—	—	—
Fair value	300	95	50	103	191	739
Asset-backed and mortgage-backed securities:						
Net carrying amount	35	11	—	130	161	337
Gross unrealized gains	—	—	—	1	1	2
Gross unrealized losses	—	—	—	1	—	1
Fair value	35	11	—	130	162	338
Total held-to-maturity investments:						
Net carrying amount	1,076	437	141	649	1,111[2]	3,414
Gross unrealized gains	7	—	1	1	6	15
Gross unrealized losses	2	—	—	10	3	15
Fair value	1,081	437	142	640	1,114	3,414
Return for the year (%)	3.61	0.12	2.10	4.21	4.34	3.33

[1] Includes obligations issued or guaranteed by Government-Sponsored Enterprises (GSE), such as debt and mortgage- and asset-backed securities, in the amount of $119 million. GSE obligations are not backed by the full faith and credit of the United States government.
[2] The net carrying amount of held-to-maturity investments held in other currencies consists of the following:

Canadian dollars	$ 851
British pounds sterling	182
Other	78
Total	$1,111

MATURITY STRUCTURE OF HELD-TO-MATURITY INVESTMENTS

December 31, 2005
Expressed in millions of United States dollars

Year of maturity	Net carrying amount	Fair value
2006	$1,432	$1,435
2007 to 2010	1,982	1,979
Total	$3,414	$3,414

ORDINARY CAPITAL
INTER-AMERICAN DEVELOPMENT BANK

APPENDIX I-3

SUMMARY STATEMENT OF LOANS – NOTE E

December 31, 2006 and 2005
Expressed in millions of United States dollars

Member in whose territory loans have been made	Outstanding 2006(1)	Currency in which outstanding balance is collectible: Non-borrowing country currencies	Borrowing country currencies	Undisbursed	Outstanding 2005(1)
Argentina	$ 8,465	$ 8,398	$ 67	$ 3,744	$ 8,474
Bahamas	74	74	—	72	71
Barbados	141	141	—	97	150
Belize	80	80	—	24	71
Bolivia	233	233	—	—	282
Brazil	11,743	11,697	46	2,310	10,820
Chile	550	549	1	201	535
Colombia	4,294	4,271	23	825	3,570
Costa Rica	535	535	—	331	569
Dominican Republic	1,067	1,067	—	430	999
Ecuador	1,326	1,326	—	404	1,286
El Salvador	1,128	1,128	—	516	1,099
Guatemala	959	959	—	537	874
Guyana	6	6	—	—	9
Honduras	104	104	—	—	120
Jamaica	565	565	—	126	594
Mexico	3,999	3,999	—	1,884	7,597
Nicaragua	84	84	—	—	92
Panama	842	842	—	457	767
Paraguay	658	658	—	452	627
Peru	3,622	3,622	—	647	3,401
Suriname	49	49	—	35	44
Trinidad and Tobago	377	377	—	192	414
Uruguay	1,837	1,837	—	605	2,230
Venezuela	1,574	1,558	16	1,059	1,723
Regional	531	531	—	46	579
Non-sovereign-guaranteed loans	1,089	1,089	—	786	1,138
Inter-American Investment Corporation	—	—	—	300	—
Total 2006	$45,932	$45,779	$153	$16,080	
Total 2005		$47,975	$160	$17,000	$48,135

(1) This table excludes outstanding participated non-sovereign-guaranteed loans which amounted to $1,205 million at December 31, 2006 (2005—$1,628 million). This table also excludes guarantees outstanding in the amount of $379 million at December 31, 2006 (2005—$319 million).

Non-sovereign-guaranteed loans outstanding have been made in the following countries (in millions):

	December 31, 2006	December 31, 2005
Argentina	$ 52	$ 141
Bolivia	93	123
Brazil	346	298
Chile	12	21
Colombia	—	10
Costa Rica	11	12
Ecuador	22	—
Jamaica	$ 30	$ 30
Mexico	236	275
Nicaragua	7	8
Panama	—	12
Peru	127	92
Uruguay	10	12
Regional	143	104
	$1,089	$1,138

ORDINARY CAPITAL
INTER-AMERICAN DEVELOPMENT BANK

APPENDIX I-4

SUMMARY STATEMENT OF LOANS OUTSTANDING BY CURRENCY AND PRODUCT – NOTE E

December 31, 2006
Expressed in millions of United States dollars

	Multicurrency loans[2]		Single currency loans			Total loans	
Currency/Rate type	Amount	Weighted average rate (%)	Amount	Weighted average rate (%)	Average maturity (years)	Amount	Weighted average rate (%)
Euro							
Fixed	$ 131	7.18	$ —	—	—	$ 131	7.18
Adjustable	1,942	4.14	14	3.72	5.65	1,956	4.14
Japanese yen							
Fixed	241	7.17	—	—	—	241	7.17
Adjustable	3,584	4.14	5	1.79	5.39	3,589	4.14
LIBOR-based floating	—	—	4	0.87	9.87	4	0.87
Swiss francs							
Fixed	138	7.21	—	—	—	138	7.21
Adjustable	2,013	4.14	—	—	—	2,013	4.14
United States dollars[1]							
Fixed	522	7.18	—	—	—	522	7.18
Adjustable	7,735	4.14	21,486	5.41	7.92	29,221	5.07
LIBOR-based fixed	—	—	584	6.72	4.03	584	6.72
LIBOR-based floating	—	—	7,378	6.72	8.30	7,378	6.72
Others							
Fixed	155	4.00	—	—	—	155	4.00
Loans outstanding							
Fixed	1,187	6.77	—	—	—	1,187	6.77
Adjustable	15,274	4.14	21,505	5.41	7.92	36,779	4.88
LIBOR-based fixed	—	—	584	6.72	4.03	584	6.72
LIBOR-based floating	—	—	7,382	6.72	8.30	7,382	6.72
Total	$16,461	4.33	$29,471	5.76	7.94	$45,932	5.25

[1] Includes loans in borrowing country currencies amounting to $74 million (2005—$19 million), which have been swapped to United States dollars.

MATURITY STRUCTURE OF LOANS OUTSTANDING

December 31, 2006
Expressed in millions of United States dollars

	Multicurrency loans[2]		Single currency loans		All loans		
Year of maturity	Fixed	Adjustable	Fixed[3]	Adjustable[3]	Fixed	Adjustable	Total
2007	$ 291	$ 1,885	$ 85	$ 2,280	$ 376	$ 4,165	$ 4,541
2008	229	1,894	76	2,100	305	3,994	4,299
2009	157	1,893	71	1,683	228	3,576	3,804
2010	133	1,817	71	1,854	204	3,671	3,875
2011	107	1,593	78	1,985	185	3,578	3,763
2012 to 2016	242	4,531	177	9,139	419	13,670	14,089
2017 to 2021	25	1,430	26	6,574	51	8,004	8,055
2022 to 2026	3	223	—	2,666	3	2,889	2,892
2027 to 2031	—	8	—	606	—	614	614
Total	$1,187	$15,274	$584	$28,887	$1,771	$44,161	$45,932
Average maturity (years)	3.10	4.92	4.03	8.02	3.41	6.95	6.81

[2] Average maturity-Multicurrency loans: The selection of currencies by the Bank for billing purposes does not permit the determination of average maturity for multicurrency loans by individual currency. Accordingly, the Bank discloses the maturity periods for its multicurrency loans and average maturity for the total multicurrency loan portfolio on a combined United States dollar equivalent basis.

[3] Includes LIBOR-based loans.

ORDINARY CAPITAL
INTER-AMERICAN DEVELOPMENT BANK

APPENDIX I-4

SUMMARY STATEMENT OF LOANS OUTSTANDING BY CURRENCY AND PRODUCT – NOTE E

December 31, 2005
Expressed in millions of United States dollars

	Multicurrency loans[2]		Single currency loans			Total loans	
Currency/Rate type	Amount	Weighted average rate (%)	Amount	Weighted average rate (%)	Average maturity (years)	Amount	Weighted average rate (%)
Euro							
Fixed	$ 154	7.27	$ —	—	—	$ 154	7.27
Adjustable	1,811	4.23	11	3.92	6.22	1,822	4.23
Japanese yen							
Fixed	328	7.25	—	—	—	328	7.25
Adjustable	3,911	4.23	3	1.60	5.89	3,914	4.23
Swiss francs							
Fixed	173	7.29	—	—	—	173	7.29
Adjustable	2,008	4.23	—	—	—	2,008	4.23
United States dollars[1]							
Fixed	729	7.26	—	—	—	729	7.26
Adjustable	8,656	4.23	23,279	4.95	8.11	31,935	4.75
LIBOR-based fixed	—	—	833	6.78	4.14	833	6.78
LIBOR-based floating	—	—	6,079	6.22	6.38	6,079	6.22
Others							
Fixed	160	4.01	—	—	—	160	4.01
Loans outstanding							
Fixed	1,544	6.93	—	—	—	1,544	6.93
Adjustable	16,386	4.23	23,293	4.95	8.11	39,679	4.65
LIBOR-based fixed	—	—	833	6.78	4.14	833	6.78
LIBOR-based floating	—	—	6,079	6.22	6.38	6,079	6.22
Total	$17,930	4.46	$30,205	5.26	7.65	$48,135	4.96

MATURITY STRUCTURE OF LOANS OUTSTANDING

December 31, 2005
Expressed in millions of United States dollars

	Multicurrency loans[2]		Single currency loans		All loans		
Year of maturity	Fixed	Adjustable	Fixed[3]	Adjustable[3]	Fixed	Adjustable	Total
2006	$ 379	$ 1,816	$110	$ 2,154	$ 489	$ 3,970	$ 4,459
2007	292	1,819	114	2,684	406	4,503	4,909
2008	225	1,824	104	2,300	329	4,124	4,453
2009	153	1,824	99	1,825	252	3,649	3,901
2010	130	1,749	97	1,881	227	3,630	3,857
2011 to 2015	334	5,360	279	8,824	613	14,184	14,797
2016 to 2020	26	1,686	30	6,450	56	8,136	8,192
2021 to 2025	5	294	—	2,737	5	3,031	3,036
2026 to 2030	—	14	—	517	—	531	531
Total	$1,544	$16,386	$833	$29,372	$2,377	$45,758	$48,135
Average maturity (years)	3.16	5.26	4.14	7.75	3.50	6.86	6.69

[1][2][3]See footnotes on previous page.

ORDINARY CAPITAL
INTER-AMERICAN DEVELOPMENT BANK

APPENDIX I-5

STATEMENT OF MEDIUM- AND LONG-TERM BORROWINGS AND SWAPS – NOTES G AND H

December 31, 2006
Expressed in millions of United States dollars

	Direct borrowings			Currency swap agreements			Interest rate swap agreements			Net currency obligations		
Currency/Rate type	Amount	Wgtd avg cost (%)	Average maturity (years)	Amount[2] payable (receivable)	Wgtd avg cost (%)	Average maturity (years)	Amount[2] payable (receivable)	Wgtd avg cost (%)	Average maturity (years)	Amount payable (receivable)	Wgtd. avg cost (%)	Average maturity (years)[1]
Euro												
Fixed	$ 2,593	5.04	3.91	$ 164	6.70	2.67	$ 196	3.65	0.89	$ 2,953	5.04	3.64
	—	—	—	(996)	5.57	2.27	(1,069)	4.15	5.34	(2,065)	4.84	3.86
Adjustable	896	5.26	7.73	3,153	3.37	3.08	1,069	3.45	5.34	5,118	3.72	4.37
	—	—	—	(896)	5.24	7.73	(196)	3.39	0.89	(1,092)	4.91	6.50
Japanese yen												
Fixed	2,463	3.03	3.31	635	0.95	1.83	42	1.71	1.37	3,140	2.59	2.98
	—	—	—	(464)	3.45	1.51	(1,115)	1.89	2.58	(1,579)	2.35	2.27
Adjustable	227	2.35	12.41	173	0.17	1.68	1,099	0.19	2.84	1,499	0.51	4.16
	—	—	—	(622)	0.90	5.75	(25)	1.23	11.83	(647)	0.91	5.98
Swiss francs												
Fixed	821	3.27	0.81	—	—	—	—	—	—	821	3.27	0.81
	—	—	—	—	—	—	—	—	—	—	—	—
Adjustable	—	—	—	616	1.42	2.94	—	—	—	616	1.42	2.94
	—	—	—	—	—	—	—	—	—	—	—	—
United States dollars												
Fixed	24,361	5.36	5.46	1,314	5.71	1.89	231	5.24	2.97	25,906	5.38	5.26
	—	—	—	(1,165)	5.68	1.19	(9,550)	4.70	6.71	(10,715)	4.81	6.11
Adjustable	150	2.46	7.73	12,906	5.20	5.59	10,786	5.14	6.54	23,842	5.16	6.03
	—	—	—	(2,558)	5.15	3.94	(1,468)	4.91	4.89	(4,026)	5.06	4.29
Others												
Fixed	14,789	6.19	5.49	—	—	—	—	—	—	14,789	6.19	5.49
	—	—	—	(14,789)	6.19	5.49	—	—	—	(14,789)	6.19	5.49
Adjustable	96	10.06	4.81	—	—	—	—	—	—	96	10.06	4.81
	—	—	—	(96)	10.06	4.81	—	—	—	(96)	10.06	4.81
Total												
Fixed	45,027	5.45	5.18	2,113			469			47,609	5.39	5.00
	—	—	—	(17,414)			(11,734)			(29,148)	5.38	5.43
Adjustable	1,369	4.81	8.30	16,848			12,954			31,171	4.64	5.60
	—	—	—	(4,172)			(1,689)			(5,861)	4.66	4.90
Principal at face value	46,396	5.43	5.27	(2,625)			—			43,771	4.96	5.16
SFAS 133 — Fair value adjustments	71			106			174			351		
Net unamortized discount	(2,437)			1,207						(1,230)		
Total	$44,030	5.43	5.27	$ (1,312)			$ 174			$42,892	4.96	5.16

(1) As of December 31, 2006, the average repricing period of the net currency obligations for adjustable rate borrowings was five months.

(2) Currency swaps are shown at face value and interest rate swaps are shown at the notional amount of each individual payable or (receivable) leg, classified by their currency. Both currency and interest rate swaps are adjusted, in total, to fair value as indicated. The net fair value amount receivable from currency swaps of $1,312 million and the net fair value amount payable from interest rate swaps of $174 million, shown in the above table, are represented by currency and interest rate swap assets at fair value of $1,880 million and currency and interest rate swap liabilities at fair value of $742 million, included on the Balance Sheet.

MATURITY STRUCTURE OF MEDIUM- AND LONG-TERM BORROWINGS OUTSTANDING

December 31, 2006
Expressed in millions of United States dollars

Year of maturity		Year of maturity	
2007	$ 6,272	2012 through 2016	$15,469
2008	6,908	2017 through 2021	2,722
2009	5,048	2022 through 2026	1,740
2010	4,893	2027	600
2011	2,744	Total	$46,396

ORDINARY CAPITAL
INTER-AMERICAN DEVELOPMENT BANK

APPENDIX I-5

STATEMENT OF MEDIUM- AND LONG-TERM BORROWINGS AND SWAPS – NOTES G AND H

December 31, 2005
Expressed in millions of United States dollars

	Direct borrowings			Currency swap agreements			Interest rate swap agreements			Net currency obligations		
Currency/Rate type	Amount	Wgtd avg cost (%)	Average maturity (years)	Amount[2] payable (receivable)	Wgtd avg cost (%)	Average maturity (years)	Amount[2] payable (receivable)	Wgtd avg cost (%)	Average maturity (years)	Amount payable (receivable)	Wgtd. avg cost (%)	Average maturity (years)[1]
Euro												
Fixed	$ 3,035	5.25	4.29	$ —	—	—	$ 412	4.22	1.31	$ 3,447	5.13	3.94
	—	—	—	(1,043)	5.28	3.98	(1,331)	3.98	4.77	(2,374)	4.55	4.42
Adjustable	711	5.38	8.19	2,246	2.16	2.18	1,331	2.66	4.77	4,288	2.85	3.98
	—	—	—	(792)	4.95	7.45	(412)	2.24	1.31	(1,204)	4.02	5.34
Japanese yen												
Fixed	2,569	3.07	4.18	765	0.93	2.82	42	1.71	2.37	3,376	2.56	3.85
	—	—	—	(468)	3.45	2.51	(1,125)	1.92	3.58	(1,593)	2.37	3.27
Adjustable	229	2.35	13.41	246	(0.28)	2.68	1,108	(0.21)	3.84	1,583	0.15	5.04
	—	—	—	(627)	0.61	6.75	(25)	1.23	12.83	(652)	0.63	6.99
Swiss francs												
Fixed	760	3.27	1.81	—	—	—	—	—	—	760	3.27	1.81
	—	—	—	—	—	—	—	—	—	—	—	—
Adjustable	—	—	—	434	0.46	3.52	—	—	—	434	0.46	3.52
	—	—	—	—	—	—	—	—	—	—	—	—
United States dollars												
Fixed	24,671	5.41	5.47	1,377	5.77	2.79	459	4.77	5.65	26,507	5.42	5.34
	—	—	—	(1,015)	5.07	1.97	(7,810)	4.60	6.99	(8,825)	4.66	6.41
Adjustable	150	2.46	8.73	12,435	4.12	5.44	9,046	4.20	6.89	21,631	4.14	6.07
	—	—	—	(1,494)	4.18	3.14	(1,695)	3.89	6.09	(3,189)	4.02	4.71
Others												
Fixed	14,195	5.97	5.33	—	—	—	—	—	—	14,195	5.97	5.33
	—	—	—	(14,195)	5.95	5.33	—	—	—	(14,195)	5.95	5.33
Adjustable	113	10.07	5.80	—	—	—	—	—	—	113	10.07	5.80
	—	—	—	(113)	10.07	5.80	—	—	—	(113)	10.07	5.80
Total												
Fixed	45,230	5.41	5.21	2,142			913			48,285	5.33	5.08
	—	—	—	(16,721)			(10,266)			(26,987)	5.19	5.48
Adjustable	1,203	4.88	9.02	15,361			11,485			28,049	3.69	5.65
	—	—	—	(3,026)			(2,132)			(5,158)	3.73	5.17
Principal at face value	46,433	5.39	5.31	(2,244)			—			44,189	4.55	5.18
SFAS 133 —												
Fair value adjustments	168			(223)			67			12		
Net unamortized discount	(2,434)			1,295						(1,139)		
Total	$44,167	5.39	5.31	$ (1,172)			$ 67			$43,062	4.55	5.18

[1] As of December 31, 2005, the average repricing period of the net currency obligations for adjustable rate borrowings was four months.

[2] Currency swaps are shown at face value and interest rate swaps are shown at the notional amount of each individual payable or (receivable) leg, classified by their currency. Both currency and interest rate swaps are adjusted, in total, to fair value as indicated. The net fair value amount receivable from currency swaps of $1,172 million and the net fair value amount payable from interest rate swaps of $67 million, shown in the above table, are represented by currency and interest rate swap assets at fair value of $1,596 million and currency and interest rate swap liabilities at fair value of $491 million, included on the Balance Sheet.

MATURITY STRUCTURE OF MEDIUM- AND LONG-TERM BORROWINGS OUTSTANDING

December 31, 2005
Expressed in millions of United States dollars

Year of maturity	
2006	$ 6,563
2007	6,091
2008	5,320
2009	4,595
2010	4,595

Year of maturity	
2011 through 2015	$14,840
2016 through 2020	2,313
2021 through 2025	1,316
2026 through 2027	800
Total	$46,433

ORDINARY CAPITAL
INTER-AMERICAN DEVELOPMENT BANK

APPENDIX I-6

STATEMENT OF SUBSCRIPTIONS TO CAPITAL STOCK – NOTE J

December 31, 2006 and 2005
Expressed in millions of United States dollars[(1)]

		Paid-in portion of subscribed capital				
Members	Shares	Freely convertible currencies	Other currencies	Callable portion of subscribed capital	Total 2006	Total 2005
Argentina	900,154	$ 361.1	$104.1	$10,393.8	$ 10,858.9	$ 10,858.9
Austria	13,312	6.9	—	153.7	160.6	160.6
Bahamas	17,398	7.5	4.1	198.3	209.9	209.9
Barbados	10,767	3.9	1.8	124.3	129.9	129.9
Belgium	27,438	14.2	—	316.8	331.0	331.0
Belize	9,178	3.6	3.6	103.5	110.7	110.7
Bolivia	72,258	29.0	8.4	834.4	871.7	871.7
Brazil	900,154	361.1	104.1	10,393.8	10,858.9	10,858.9
Canada	334,887	173.7	—	3,866.2	4,039.9	4,039.9
Chile	247,163	99.1	28.6	2,853.9	2,981.6	2,981.6
Colombia	247,163	99.2	28.6	2,853.9	2,981.6	2,981.6
Costa Rica	36,121	14.5	4.2	417.1	435.7	435.7
Croatia	4,018	2.1	—	46.4	48.5	48.5
Denmark	14,157	7.3	—	163.4	170.8	170.8
Dominican Republic	48,220	19.3	5.6	556.8	581.7	581.7
Ecuador	48,220	19.3	5.6	556.8	581.7	581.7
El Salvador	36,121	14.5	4.2	417.1	435.7	435.7
Finland	13,312	6.9	—	153.7	160.6	160.6
France	158,638	82.3	—	1,831.4	1,913.7	1,913.7
Germany	158,638	82.3	—	1,831.4	1,913.7	1,913.7
Guatemala	48,220	19.3	5.6	556.8	581.7	581.7
Guyana	13,393	5.2	2.6	153.8	161.6	161.6
Haiti	36,121	14.5	4.2	417.1	435.7	435.7
Honduras	36,121	14.5	4.2	417.1	435.7	435.7
Israel	13,126	6.8	—	151.5	158.3	158.3
Italy	158,638	82.3	—	1,831.4	1,913.7	1,913.7
Jamaica	48,220	19.3	5.6	556.8	581.7	581.7
Japan	418,642	217.1	—	4,833.2	5,050.3	5,050.3
Korea, Republic of	184	0.1	—	2.1	2.2	2.2
Mexico	578,632	232.1	66.9	6,681.3	6,980.3	6,980.3
Netherlands	28,207	14.6	—	325.6	340.3	340.3
Nicaragua	36,121	14.5	4.2	417.1	435.7	435.7
Norway	14,157	7.3	—	163.4	170.8	170.8
Panama	36,121	14.5	4.2	417.1	435.7	435.7
Paraguay	36,121	14.5	4.2	417.1	435.7	435.7
Peru	120,445	48.3	14.0	1,390.7	1,453.0	1,453.0
Portugal	4,474	2.3	—	51.7	54.0	54.0
Slovenia	2,434	1.3	—	28.1	29.4	29.4
Spain	158,638	82.3	—	1,831.4	1,913.7	1,913.7
Suriname	7,342	3.5	2.2	82.9	88.6	88.6
Sweden	27,268	14.1	—	314.8	328.9	328.9
Switzerland	39,347	20.4	—	454.2	474.7	474.7
Trinidad and Tobago	36,121	14.5	4.2	417.1	435.7	435.7
United Kingdom	80,551	41.8	—	929.9	971.7	971.7
United States	2,512,529	1,303.0	—	29,006.7	30,309.7	30,309.7
Uruguay	96,507	38.7	11.2	1,114.3	1,164.2	1,164.2
Venezuela	482,267	216.0	33.3	5,568.5	5,817.8	5,817.8
Total before unallocated amount	8,367,264	3,870.6	468.8	96,598.5	100,937.9	100,937.9
Unallocated[(2)]	1,299	0.9	—	14.8	15.7	15.7
Total 2006	8,368,563	$ 3,871	$ 469	$ 96,613	$ 100,953	
Total 2005	8,368,563	$ 3,871	$ 469	$ 96,613		$ 100,953

[(1)] Data are rounded; detail may not add up to subtotals and totals because of rounding.
[(2)] Represents the remaining shares of the former Socialist Federal Republic of Yugoslavia.

ORDINARY CAPITAL
INTER-AMERICAN DEVELOPMENT BANK

APPENDIX I-7

STATEMENT OF SUBSCRIPTIONS TO CAPITAL STOCK AND VOTING POWER

December 31, 2006

Member countries	Subscribed shares	Number of votes	% of total number of votes[1]
Regional developing members			
Argentina	900,154	900,289	10.752
Bahamas	17,398	17,533	0.209
Barbados	10,767	10,902	0.130
Belize	9,178	9,313	0.111
Bolivia	72,258	72,393	0.865
Brazil	900,154	900,289	10.752
Chile	247,163	247,298	2.953
Colombia	247,163	247,298	2.953
Costa Rica	36,121	36,256	0.433
Dominican Republic	48,220	48,355	0.577
Ecuador	48,220	48,355	0.577
El Salvador	36,121	36,256	0.433
Guatemala	48,220	48,355	0.577
Guyana	13,393	13,528	0.162
Haiti	36,121	36,256	0.433
Honduras	36,121	36,256	0.433
Jamaica	48,220	48,355	0.577
Mexico	578,632	578,767	6.912
Nicaragua	36,121	36,256	0.433
Panama	36,121	36,256	0.433
Paraguay	36,121	36,256	0.433
Peru	120,445	120,580	1.440
Suriname	7,342	7,477	0.089
Trinidad and Tobago	36,121	36,256	0.433
Uruguay	96,507	96,642	1.154
Venezuela	482,267	482,402	5.761
Total regional developing members	4,184,669	4,188,179	50.016
Canada	334,887	335,022	4.001
United States	2,512,529	2,512,664	30.007
Nonregional members			
Austria	13,312	13,447	0.161
Belgium	27,438	27,573	0.329
Croatia	4,018	4,153	0.050
Denmark	14,157	14,292	0.171
Finland	13,312	13,447	0.161
France	158,638	158,773	1.896
Germany	158,638	158,773	1.896
Israel	13,126	13,261	0.158
Italy	158,638	158,773	1.896
Japan	418,642	418,777	5.001
Korea, Republic of	184	319	0.004
Netherlands	28,207	28,342	0.338
Norway	14,157	14,292	0.171
Portugal	4,474	4,609	0.055
Slovenia	2,434	2,569	0.031
Spain	158,638	158,773	1.896
Sweden	27,268	27,403	0.327
Switzerland	39,347	39,482	0.472
United Kingdom	80,551	80,686	0.964
Total nonregional members	1,335,179	1,337,744	15.976
Total before unallocated amount	8,367,264	8,373,609	100.000
Unallocated[2]	1,299	1,434	
GRAND TOTAL	8,368,563	8,375,043	

[1] Data are rounded; detail may not add to subtotals and grand total because of rounding.
[2] Represents the remaining shares of the former Socialist Federal Republic of Yugoslavia.

SPECIAL PURPOSE FINANCIAL STATEMENTS

FUND FOR SPECIAL OPERATIONS

REPORT OF INDEPENDENT AUDITORS

Board of Governors
Inter-American Development Bank

We have audited the accompanying special purpose statement of assets, liabilities and fund balance of the Inter-American Development Bank (Bank)—Fund for Special Operations (FSO) as of December 31, 2006 and 2005, and the related special purpose statements of changes in general reserve (deficit), comprehensive income, and cash flows for each of the three years in the period ended December 31, 2006. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform an audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the FSO's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the FSO's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described in Note B, the accompanying special purpose financial statements have been prepared for the purpose of complying with Article IV, Section 8(d) of the Agreement Establishing the Inter-American Development Bank, and are not intended to be a presentation in conformity with United States generally accepted accounting principles.

In our opinion, the accompanying special purpose financial statements of the Inter-American Development Bank—Fund for Special Operations as of December 31, 2006 and 2005 and for each of the three years in the period ended December 31, 2006, present fairly, in all material respects, the information set forth therein on the basis of accounting described in Note B.

This report was prepared solely for the information and use of the Board of Governors, Board of Executive Directors, and management of the Inter-American Development Bank. However, under the Agreement Establishing the Inter-American Development Bank, this report is included in the Annual Report of the Bank and is therefore a matter of public record and its distribution is not limited.

Ernst + Young LLP

Washington, D.C.
February 6, 2007

FUND FOR SPECIAL OPERATIONS
INTER-AMERICAN DEVELOPMENT BANK

SPECIAL PURPOSE STATEMENT OF ASSETS, LIABILITIES AND FUND BALANCE

Expressed in millions of United States dollars

	December 31,			
	2006		2005	
ASSETS				
Cash and investments				
Cash	$ 389		$ 378	
Investments	1,203	$1,592	1,182	$1,560
Loans outstanding		7,115		6,873
Accrued interest and other charges				
On investments	—		4	
On loans	39	39	38	42
Receivable from members				
Non-negotiable, non-interest-bearing demand obligations	567		628	
Amounts required to maintain value of currency holdings	209	776	272	900
Receivable for investment securities sold		—		4
Other assets		8		7
Total assets		$9,530		$9,386
LIABILITIES AND FUND BALANCE				
Liabilities				
Accounts payable and accrued expenses	$ 6		$ 11	
Undisbursed technical cooperation projects and other financings	84		94	
Amounts payable to maintain value of currency holdings	300	$ 390	240	$ 345
Fund balance				
Contribution quotas authorized and subscribed	9,725		9,671	
General reserve (deficit)	(583)		(627)	
Accumulated translation adjustments	(2)	9,140	(3)	9,041
Total liabilities and fund balance		$9,530		$9,386

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

FUND FOR SPECIAL OPERATIONS
INTER-AMERICAN DEVELOPMENT BANK

SPECIAL PURPOSE STATEMENT OF CHANGES IN GENERAL RESERVE (DEFICIT)

Expressed in millions of United States dollars

	Years ended December 31,		
	2006	**2005**	**2004**
Income			
Loans			
Interest	**$ 139**	$ 135	$ 131
Other loan income	**13**	14	14
	152	149	145
Investments	**60**	38	21
Total income	**212**	187	166
Expenses			
Administrative expenses	**93**	86	62
Total expenses	**93**	86	62
Excess of income over expenses before technical cooperation expense and HIPC debt relief	**119**	101	104
Technical cooperation expense	**19**	28	31
HIPC debt relief	**(5)**	76	486
Excess of income over expenses (expenses over income)	**105**	(3)	(413)
General reserve (deficit), beginning of year	**(627)**	(562)	(76)
Allocations to Intermediate Financing Facility Account	**(61)**	(62)	(73)
General reserve (deficit), end of year	**$(583)**	$(627)	$(562)

SPECIAL PURPOSE STATEMENT OF COMPREHENSIVE INCOME

Expressed in millions of United States dollars

	Years ended December 31,		
	2006	**2005**	**2004**
Excess of income over expenses (expenses over income)	**$105**	$ (3)	$(413)
Translation adjustments on assets and liabilities	**54**	(89)	57
Comprehensive income (loss)	**$159**	$(92)	$(356)

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

FUND FOR SPECIAL OPERATIONS
INTER-AMERICAN DEVELOPMENT BANK

SPECIAL PURPOSE STATEMENT OF CASH FLOWS

Expressed in millions of United States dollars

	Years ended December 31,		
	2006	**2005**	**2004**
Cash flows from lending activities			
Lending:			
Loan disbursements	**$ (398)**	$ (424)	$ (463)
Loan collections	**290**	301	294
Loan participations, net	**(2)**	(1)	—
Net cash used in lending activities	**(110)**	(124)	(169)
Cash flows from financing activities			
Collections of receivable from members	**101**	130	150
Net cash provided by financing activities	**101**	130	150
Cash flows from operating activities			
Gross purchases of investments	**(1,208)**	(2,269)	(2,527)
Gross proceeds from sale or maturity of investments	**1,233**	2,237	2,556
Loan income collections	**152**	146	136
Income from investments	**26**	38	19
Administrative expenses	**(99)**	(77)	(83)
Technical cooperation and other financings	**(29)**	(34)	(31)
Net cash provided by operating activities	**75**	41	70
Cash allocations to the Intermediate Financing Facility Account	**(61)**	(62)	(73)
Effect of exchange rate fluctuations on cash	**6**	6	5
Net increase (decrease) in Cash	**11**	(9)	(17)
Cash, beginning of year	**378**	387	404
Cash, end of year	**$ 389**	$ 378	$ 387

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

FUND FOR SPECIAL OPERATIONS
INTER-AMERICAN DEVELOPMENT BANK

NOTES TO SPECIAL PURPOSE FINANCIAL STATEMENTS

Note A – Origin
The Inter-American Development Bank (Bank) is an international organization which was established in December 1959. Its principal purpose is to promote the economic and social development of Latin America and the Caribbean, primarily by providing loans and related technical assistance for specific projects and for programs of economic reform. The Fund for Special Operations (FSO) was established under the Agreement Establishing the Inter-American Development Bank (Agreement) to make loans on highly concessional terms in the less developed member countries of the Bank. The FSO also provides technical assistance both related to projects and not connected to specific loans. The FSO complements the activities of the Ordinary Capital and the Intermediate Financing Facility Account (IFF). The IFF's purpose is to subsidize part of the interest payments for which certain borrowers are liable on loans from the Ordinary Capital. The FSO makes annual general reserve allocations to the IFF, as indicated in Note H.

Note B – Summary of Significant Accounting Policies
Due to the nature and organization of the FSO, the accompanying financial statements have been prepared on a special accounting basis. As described below, this special accounting basis is not consistent with United States generally accepted accounting principles (GAAP) with respect to certain items. These special purpose financial statements have been prepared to comply with Article IV, Section 8(d) of the Agreement.

Basis of accounting
The special purpose financial statements are prepared on the accrual basis of accounting for loan income, investment income and administrative expenses. That is, the effect of transactions and other events is recognized when they occur (not as cash is received or paid) and they are recorded in the accounting records and reported in the annual financial statements of the period to which they relate. The FSO follows a special accounting basis for loans and contribution quotas as described below.

Use of estimates
The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Translation of currencies
The financial statements are expressed in United States dollars; however, the Bank conducts its operations in the currencies of all of its members, which are considered functional currencies. The FSO resources are derived from contribution quotas and accumulated earnings in those various currencies. Assets and liabilities denominated in currencies other than the United States dollar are translated at market exchange rates prevailing at the dates of the Special Purpose Statement of Assets, Liabilities and Fund Balance. Income and expenses in such currencies are translated at market rates of exchange prevailing during each month. Exchange rate fluctuations do not have any effect on the United States dollar equivalents of currencies subject to the maintenance of value (MOV) provision described below. Net adjustments resulting from the translation into United States dollars of assets and liabilities in currencies that do not have MOV protection, which are derived from the 1983, 1990 and 1995 increases in contribution quotas, are presented as a component of Comprehensive income (loss)[1] in the Special Purpose Statement of Comprehensive Income. The adjustments resulting from the translation of contribution quotas authorized and subscribed that do not have MOV protection are charged or credited directly to Accumulated translation adjustments in the Special Purpose Statement of Assets, Liabilities and Fund Balance. Under United States GAAP, the contribution quotas authorized and subscribed should be reported at the historical rates of exchange prevailing at the date of payment.

Investments
Investment securities are recorded using trade-date accounting and are held in a trading portfolio carried at fair value, with changes in fair value included in Income from investments.

Loans
The Bank utilizes FSO resources to make highly concessional loans, denominated in the currencies of non-borrowing member countries, to the least-developed borrowing members, their agencies or political subdivisions. In previous years, the Bank also made concessional loans in local currencies to borrowing members. In the case of loans to borrowers other than national governments, central banks or other governmental or intergovernmental entities, the Bank follows the general policy of requiring a guarantee engaging the full faith and credit of the government. Under the loan contracts with the borrowers, the Bank sells participations in certain loans to the Social Progress Trust Fund, reserving to itself the administration of those loans.

Loans generally have up to 40 years final maturity and up to a 10 year grace period for principal payments, and generally

[1]References to captions in the special purpose financial statements are identified by the name of the caption beginning with a capital letter every time they appear in the notes to the special purpose financial statements.

FUND FOR SPECIAL OPERATIONS
INTER-AMERICAN DEVELOPMENT BANK

NOTES TO SPECIAL PURPOSE FINANCIAL STATEMENTS (continued)

carry an interest rate of 1% during the grace period and 2% thereafter. The principal amount of loans and accrued interest are repayable in the currencies lent.

It is the policy of the Bank to place on nonaccrual status all loans to a member government if service under any loan to, or guaranteed by, the member government, made from any fund owned or administered by the Bank, is overdue more than 180 days. On the date that a member's loan is placed on nonaccrual status, all loans to that member country are also placed on nonaccrual status. When a loan is placed on nonaccrual status, charges that had been accrued and remain unpaid are deducted from the income of the current period. Charges on nonaccruing loans are included in income only to the extent that payments have actually been received. On the date a member pays in full all overdue amounts, the member's loans emerge from nonaccrual status, its eligibility for new loans is restored, and all overdue charges (including those from prior years) are recognized as income from loans in the current period. Except for the debt relief loan write-offs resulting from the implementation of the Heavily Indebted Poor Countries (HIPC) Initiative discussed in Note M, the Bank has never had a write-off on any of its FSO loans and has a policy of not rescheduling loan repayments.

Incremental direct costs associated with originating loans are expensed as incurred as such amounts are immaterial to the financial results.

Under United States GAAP, loans are recorded at their net realizable value, including an allowance for amounts estimated to be uncollectible. Management has elected to present loans under a special accounting basis to provide for recording loans and accrued interest at the full face amount of the borrowers' outstanding obligations. Any loan losses that might occur would be charged to income of the current period.

The principal component of loans affected by the Enhanced HIPC Initiative is recognized as HIPC debt relief in the Special Purpose Statement of Changes in General Reserve (Deficit), and as a reduction in Loans outstanding in the Special Purpose Statement of Assets, Liabilities and Fund Balance, when the Board of Executive Directors determines that a country has reached completion point. Interim debt relief, which is revocable, during the period between decision and completion point (as defined in Note M) is recognized when relief is delivered to the country. HIPC loans continue to accrue interest and other charges until principal debt relief is delivered. The interest and other charges component of debt relief, if any, is recognized as HIPC debt relief in the period it is forgiven.

Receivable from members
Receivable from members includes non-negotiable, non-interest bearing demand obligations that have been accepted in lieu of the immediate payment of all or any part of a member's contribution quotas and MOV obligations.

Contribution quotas
Recognition: Under United States GAAP, contribution quotas authorized and subscribed should not be recorded until a promissory demand note is received, guaranteed by the member country, as payment of the amount due. To present the full amount of the member country's commitment, management has elected to report contribution quotas under a special accounting basis that provides for the recording of member's contribution quotas in full as contribution quotas receivable upon approval of the relevant replenishment by the Board of Governors.

Contribution quotas come due as a receivable throughout the replenishment period in accordance with an agreed-upon subscription and encashment schedule. The actual subscription and payment of receivables when they become due from certain members is conditional upon the respective member's budgetary appropriation processes. Contribution quotas are settled through payment of cash or non-negotiable, non-interest-bearing demand notes. Notes received in settlement of contribution quotas are encashed as provided in the relevant replenishment resolution.

Valuation: The Agreement provides that contribution quotas be expressed in terms of the United States dollar of the weight and fineness in effect on January 1, 1959. The Second Amendment to the Articles of Agreement of the International Monetary Fund eliminated par values of currencies in terms of gold effective April 1, 1978. Consequently, the General Counsel of the Bank rendered an opinion that the Special Drawing Right (SDR) became the successor to the 1959 United States dollar as the standard of value for member contributions, and for maintaining the value of the FSO's currency holdings. The SDR has a value equal to the sum of the values of specific amounts of stated currencies, including the United States dollar. Pending a decision by the Bank's governing board and as suggested in the General Counsel's opinion, the Bank is continuing its practice of using as the basis of valuation the 1959 United States dollar, as valued in terms of United States dollars at July 1, 1974, whose value is equal to approximately 1.2063 of the then current United States dollars.

Maintenance of value
In accordance with the Agreement, each member is required to maintain the value of its currency held in the FSO to the extent established by the terms for the respective increases in contribution quotas. Likewise, and subject to the same terms of the contribution quota increases, the Bank is required to return to a member

FUND FOR SPECIAL OPERATIONS
INTER-AMERICAN DEVELOPMENT BANK

NOTES TO SPECIAL PURPOSE FINANCIAL STATEMENTS (continued)

an amount of its currency equal to any significant increase in value of such member's currency held in the FSO. The standard of value for these purposes is the United States dollar of the weight and fineness in effect on January 1, 1959. Currency holdings derived from the 1983, 1990 and 1995 increases in contribution quotas do not have MOV protection.

The amount related to MOV on non-borrowing member countries currency holdings is presented as an asset or liability on the Special Purpose Statement of Assets, Liabilities and Fund Balance, included in Amounts required/payable to maintain value of currency holdings.

Administrative expenses
Substantially all administrative expenses of the Bank, including depreciation, are allocated between the FSO and the Ordinary Capital, pursuant to an allocation method approved by the Board of Executive Directors. Following this allocation method, during 2006 the effective ratio of administrative expenses charged to the FSO was 18.7% and 81.3% to the Ordinary Capital (2005—18.5% and 81.5%; 2004—15.6% and 84.4%).

Technical cooperation
Non-reimbursable technical cooperation projects, as well as certain financings whose recovery is explicitly contingent on events that may not occur, are recorded as Technical cooperation expense at the time of approval.

Cancellations of undisbursed balances and recuperations of contingently recoverable financings are recognized as an offset to Technical cooperation expense in the period in which they occur.

Fair values of financial instruments
The following methods and assumptions were used by the Bank in estimating the fair value for its financial instruments:

Cash: The carrying amount reported in the Special Purpose Statement of Assets, Liabilities and Fund Balance for cash approximates fair value.

Investments: Fair values for investment securities are based on quoted market prices, where available; otherwise they are based on dealer prices of comparable instruments or discounted cash flows.

Loans: The Bank is one of very few sources of development loans to Latin American and Caribbean countries. There is no secondary market for development loans. Interest on all loans is accrued at fixed rates. For all loans and related commitments, the Bank is of the opinion that, due to its unique position in lending operations and the absence of a secondary market, it is not practicable to estimate a fair value for its lending portfolio.

Note C – Restricted Currencies
As of December 31, 2006, Cash includes $377 million (2005—$368 million) in currencies of regional borrowing members. The amount of $43 million (2005—$36 million) has been restricted by one member in accordance with provisions of the Agreement, to be used for making payments for goods and services produced in its territory.

Note D – Investments
As part of its overall portfolio management strategy, the Bank invests FSO resources both directly and indirectly, through an investment pool managed by the Bank, in high quality securities in accordance with established investment guidelines. FSO investments include government, agency, corporate and bank obligations, and asset-backed and mortgage-backed securities with credit ratings ranging from AAA to A+ (short-term securities carry the highest short-term credit ratings). The Bank limits its activities of investing in securities to a list of authorized dealers and counterparties. Credit limits have been established for each counterparty.

A summary of the trading portfolio securities at December 31, 2006 and 2005 is shown in the Summary Statement of Investments in Appendix II-1. The average return on investments, including realized and unrealized gains and losses, during 2006 was 5.04% (2005—3.09%; 2004—1.83%).

Note E – Loans Outstanding
Approved loans are disbursed to borrowers in accordance with the requirements of the project being financed; however, disbursements do not begin until the borrower and guarantor, if any, fulfill certain conditions precedent as required by contract. Loans outstanding by country are shown in the Summary Statement of Loans Outstanding in Appendix II-2. The average interest rate for loans outstanding at December 31, 2006 and 2005 was 1.74% and 1.73%, respectively, and the average maturity was 13.9 years, in both years.

Note F – Receivable from Members
The composition of the net receivable from members as of December 31, 2006 and 2005 is as follows (in millions):

	2006	2005
Regional developing members	$ 751	$ 849
Canada	4	2
Non-regional members	(279)	(191)
Total	$ 476	$ 660

FUND FOR SPECIAL OPERATIONS
INTER-AMERICAN DEVELOPMENT BANK

NOTES TO SPECIAL PURPOSE FINANCIAL STATEMENTS (continued)

These amounts are represented on the Special Purpose Statement of Assets, Liabilities and Fund Balance as follows (in millions):

	2006	2005
Receivable from members	$ 776	$ 900
Amounts payable to maintain value of currency holdings	(300)	(240)
Total	$ 476	$ 660

Note G – Contribution Quotas Authorized and Subscribed

Non-negotiable, non-interest-bearing demand obligations have been accepted in lieu of the immediate payment of all or any part of a member's contribution quotas. The payment of contribution quotas is conditional on the members' budgetary and, in some cases, legislative processes. The Canadian contribution quota is being increased by collections of principal, interest and service charges on loans extended from the Canadian Trust Fund administered by the Bank. For a Statement of Contribution Quotas at December 31, 2006 and 2005, see Appendix II-3.

Changes for the period

The following table summarizes the changes in Contribution quotas authorized and subscribed for the years ended December 31, 2006 and 2005 (in millions):

	Contribution quotas authorized and subscribed
Balance at January 1, 2005	$9,802
Contribution by Canada— Trust Fund collections	1
Translation adjustment of contributions approved in 1983, 1990 and 1995 due to exchange rate fluctuations	(132)
Balance at December 31, 2005	9,671
Contribution by Canada— Trust Fund collections	1
Translation adjustment of contributions approved in 1983, 1990 and 1995 due to exchange rate fluctuations	53
Balance at December 31, 2006	$9,725

As of December 31, 2006, the cumulative decrease in the United States dollar equivalents of contribution quotas because of exchange rate fluctuations was $59 million (2005—$112 million).

Voting power

In making decisions concerning operations of the FSO, the number of votes and percent of voting power for each member country are the same as those applicable for decisions involving the Ordinary Capital.

Note H – General Reserve (Deficit)

In accordance with resolutions of the Board of Governors, the excess of income over expenses is to be added to the general reserve.

In 2006, the Board of Governors allocated the equivalent of $61 million (2005—$62 million; 2004—$73 million) in convertible currencies from the general reserve of the FSO to the IFF to subsidize part of the interest for which certain borrowers are liable on loans from the Ordinary Capital. Projected allocations, in accordance with various agreements of the Board of Governors, are shown in the following table (in millions):

Year	Capital increases[(1)]	HIPC Initiative[(2)]	Concessional resources agreement[(3)]	Total
2007	$ 30	$11	$ 20	$ 61
2008	30	11	20	61
2009	30	11	20	61
2010	30	6	20	56
2011	30	—	20	50
2012 to 2016	—	—	360	360
2017 to 2019	—	—	195	195
Total	$150	$39	$655	$844

(1) Under the terms of the Sixth and Seventh General Capital Increases in the Resources of the Bank.

(2) Transfers to fund additional subsidy payments on Ordinary Capital loans to Bolivia and Guyana. See Note M for a description of the HIPC Initiative.

(3) Mandated allocations under the Concessional resources agreement approved by the Board of Governors in 1999 amount to $20 million annually from 2000 to 2012 and $15 million in 2013. Additional transfers of approximately $65 million annually from 2012 to 2019 will be necessary to fund the 2000–2008 IFF lending mandated under the Concessional resources agreement. The level of these additional transfers may change as assumptions are revised in future years.

These allocations are subject to annual approvals by the Board of Governors and to adjustment for appropriate reasons related to the availability of funding for the IFF. See Note N for possible impact of the proposed New Debt Relief Structure and Concessional Lending Framework on future allocations.

FUND FOR SPECIAL OPERATIONS
INTER-AMERICAN DEVELOPMENT BANK

NOTES TO SPECIAL PURPOSE FINANCIAL STATEMENTS (continued)

The following is a summary of changes in the General reserve (deficit) for the years ended December 31, 2006 and 2005 (in millions):

	HIPC Initiative	Income, other than HIPC	Total General reserve (deficit)
Balance at January 1, 2005	$(1,320)	$758	$(562)
Allocation to IFF	(1)	(61)	(62)
HIPC debt relief	(76)	—	(76)
Income, excluding HIPC	—	73	73
Balance at December 31, 2005	(1,397)	770	(627)
Allocation to IFF	—	(61)	(61)
HIPC debt relief	5	—	5
Income, excluding HIPC	—	100	100
Balance at December 31, 2006	$(1,392)	$809	$(583)

Note I – Accumulated Translation Adjustments

The following is a summary of changes in the Accumulated translation adjustments for the years ended December 31, 2006 and 2005 (in millions):

	Assets and liabilities	Contribution quotas authorized and subscribed	Total
Balance at January 1, 2005	$ (26)	$ (20)	$(46)
Translation adjustments	(89)	132	43
Balance at December 31, 2005	(115)	112	(3)
Translation adjustments	54	(53)	1
Balance at December 31, 2006	$ (61)	$ 59	$ (2)

Note J – Administrative Expenses

Pursuant to the policy described in Note B, the FSO shares in all of the expenses incurred by the Bank, including those related to the pension and postretirement benefit plans.

Note K – Undisbursed Technical Cooperation Projects and Other Financings

The following is a summary of changes in Undisbursed technical cooperation projects and other financings for the years ended December 31, 2006 and 2005 (in millions):

	2006	2005
Balance at January 1,	$ 94	$ 99
Approvals	28	36
Cancellations	(6)	(5)
Disbursements	(32)	(36)
Balance at December 31,	$ 84	$ 94

Note L – Reconciliation of Excess of Income over Expenses (Expenses over Income) to Net Cash Provided by Operating Activities

A reconciliation of Excess of income over expenses (expenses over income) to Net cash provided by operating activities, as shown in the Special Purpose Statement of Cash Flows, is as follows (in millions):

	Years ended December 31,		
	2006	2005	2004
Excess of income over expenses (expenses over income)	$105	$ (3)	$(413)
Difference between amounts accrued and amounts paid or collected for:			
Loan income	—	(3)	(8)
Income from investments	4	—	(2)
Net unrealized gain on investments	(39)	—	—
Administrative expenses	(6)	9	(21)
Technical cooperation and other financings	(9)	(6)	(1)
Net decrease (increase) in investments	25	(32)	29
HIPC debt relief	(5)	76	486
Net cash provided by operating activities	$ 75	$ 41	$ 70
Supplemental disclosure of noncash activities			
Increase (decrease) resulting from exchange rate fluctuations:			
Investments	$ 4	$ (18)	$ 15
Loans outstanding	128	(217)	131
Receivable from members-net	(84)	142	(94)
Contribution quotas authorized and subscribed	53	(132)	66

Note M – Heavily Indebted Poor Countries Initiative

The Bank participates in the HIPC Initiative, a concerted international initiative endorsed by the Group of Seven Countries (G-7), the International Bank for Reconstruction and Development (the World Bank) and the International Monetary Fund, for addressing the debt problems of a group of countries identified as heavily indebted poor countries to ensure that reform efforts of these countries will not be put at risk by continued high external debt burdens. Under the HIPC Initiative, all bilateral and multilateral creditors are providing debt relief for countries that demonstrate good policy performance over an extended period in order to bring their debt service burdens to sustainable levels.

The Bank's participation in the HIPC comprises the HIPC I approved in 1998 and the Enhanced HIPC Initiative approved in 2001. At December 31, 2006, eligible member countries were Bolivia, Guyana, Honduras and Nicaragua. In January 2007, the Board of Governors approved Haiti's eligibility under the Enhanced HIPC Initiative. Haiti, which has reached decision point, is expected to receive debt relief under this initiative in the amount of $60.4 million in net present value terms. Total debt relief under this initiative is expected to amount to a net present value, calculated as of the HIPC effective date for each country, of approximately $1.2 billion. This debt relief, which is being delivered from 1998 through 2019, is being implemented through a combination of write-offs of FSO loans' principal and interest, transfers from the FSO general reserve to the IFF, conversion of a substantial amount of FSO local currency holdings to United States dollars, and grants of member countries through the World Bank HIPC Trust Fund.

As part of HIPC I, in 1998 the Bank charged off FSO loans to Bolivia and Guyana in the amount of $177.1 million. In addition, the Bank is transferring the equivalent of $138 million in convertible currencies during the period 1998 to 2010 from the FSO's general reserve to the IFF to provide for increased IFF subsidy payments during the period 1998 to 2015 on Ordinary Capital loans. Of this amount, $99 million had already been transferred as of December 31, 2006.

Enhanced HIPC Initiative

As part of the Enhanced HIPC Initiative, the Bank delivers debt service relief by forgiving a portion of an eligible country's debt service obligations as they become due. Additional debt service relief, being delivered from 2001 to 2008, is funded by amounts received from the World Bank HIPC Trust Fund. Such amounts, including any investment income thereon, are kept separately from the resources of the FSO in the HIPC Account, and are used solely for the specific purpose of meeting debt service obligations of eligible countries. These resources are not included in the financial statements and do not affect the operations of the FSO.

Under the Enhanced HIPC Initiative, decision point is reached once the country has established an adequate policy track record. The completion point is achieved once the country has demonstrated continued strong policy performance. During the period between decision point and completion point, referred to as the interim period, partial debt relief, not to exceed one-third of the total relief amount, may be granted to a country. Such interim debt relief is revocable and is contingent upon the country making satisfactory progress towards a strong policy performance. Once a country reaches completion point, the debt relief to the country becomes irrevocable.

Because of its revocable nature, interim debt relief is recognized only when actual relief is delivered to the country. Once the Board of Executive Directors determines that a country has reached completion point, the remaining nominal value of the principal component of the total debt relief to be provided to the country is recorded as a reduction in Loans outstanding in the Special Purpose Statement of Assets, Liabilities and Fund Balance and as HIPC debt relief in the Special Purpose Statement of Changes in General Reserve (Deficit). The interest and other charges component of debt relief, if any, is recognized as HIPC debt relief in the period the debt relief is delivered and adjustments to previously recognized amounts, if any, when determined.

Guyana and Nicaragua reached completion point in 2004 and Honduras in 2005. Upon reaching completion point, HIPC debt relief of $64 million, $409 million and $85 million, respectively, was recognized representing the estimated nominal value of the principal component of the total debt relief remaining to be delivered to each country.

During 2006, 2005 and 2004, the following amounts of HIPC debt relief were recognized as per the accounting policy described above (in millions):

Country	HIPC status as of December 31, 2006	HIPC Debt Relief 2006	2005	2004
Bolivia.	Completion	$(2)	$ (4)	$ (5)
Honduras	Completion	(4)	85	—
Guyana	Completion	—	(1)	68
Nicaragua	Completion	1	(4)	423
Total		$(5)	$ 76	$486

Note N – New Debt Relief Structure and Concessional Lending Framework

The World Bank's International Development Agency, the International Monetary Fund and the African Development Fund have approved their participation in the Multilateral Debt Relief Initiative (MDRI) to provide additional debt relief to HIPC countries. Although the MDRI does not include the Bank, the Bank's Board of Governors has supported the principle of furthering FSO debt relief for HIPC-eligible countries in Latin America and the Caribbean.

In December 2006, the Board of Governors approved a structure including one hundred (100) percent relief of eligible FSO debt for Bolivia, Guyana, Haiti, Honduras and Nicaragua,

FUND FOR SPECIAL OPERATIONS
INTER-AMERICAN DEVELOPMENT BANK

NOTES TO SPECIAL PURPOSE FINANCIAL STATEMENTS (continued)

effective January 1, 2007, as well as (i) the continuance of the access to concessional resources for FSO countries (other than Haiti) via a blending of loans from the FSO and the Ordinary Capital ("parallel loans"), (ii) Haiti's access to an appropriate mix of loans and/or grants with adequate levels of concessionality, (iii) the IFF's extension to 2015 via a blending of FSO resources and Ordinary Capital loans, and (iv) annual non-reimbursable technical assistance of $30 million.

To implement this structure for further debt relief, in January 2007 the Committee of the Board of Governors agreed to submit a proposal to the Board of Governors identifying as such eligible FSO debt the approximate principal amount of $3.4 billion in outstanding FSO loan balances as of December 31, 2004, subject to the Board of Executive Directors' approval of a reform proposal presented by management on the future operations of the FSO. If approved, inter alia, the FSO would bear a smaller percentage of the administrative expenses of the Bank currently allocated between the Ordinary Capital and the FSO; and countries eligible for IFF subsidies would continue to receive concessional resources for new loans through 2015, in the form of parallel loans rather than a reduction in the interest rate billed, and would still receive the reduction in interest rate billed for existing loans, even though FSO transfers to the IFF (as contemplated in Note H) would not reoccur before 2014. A vote on the proposal is expected in the first quarter of 2007.

Following the recognition criteria under the FSO's accounting policies, this further debt relief would be reflected in the financial statements of the FSO in full in 2007, except for debt relief for Haiti, as a reduction of Loans outstanding and as an expense in the Special Purpose Statement of Changes in General Reserve (Deficit) after the Board of Governors approves the proposal. Further debt relief for Haiti would similarly be reflected in the financial statements of the FSO in full once Haiti reaches the completion point for the Enhanced HIPC Initiative.

FUND FOR SPECIAL OPERATIONS
INTER-AMERICAN DEVELOPMENT BANK

APPENDIX II-1

SUMMARY STATEMENT OF INVESTMENTS – NOTE D

December 31, 2006 and 2005
Expressed in millions of United States dollars

Investments	2006	2005
Investment Pool	$1,097	$ —
Obligations of the United States Government and its corporations and agencies	—	166
Obligations of other governments and agencies	—	63
Bank obligations	106	186
Corporate securities	—	59
Asset-backed and mortgage-backed securities	—	708
	$1,203	$1,182

The currencies of the above investments are as follows:

Currencies	2006	2005
British pounds sterling	$ 14	$ 65
Canadian dollars	14	—
Euro	38	14
Swedish kronor	2	—
Swiss francs	1	—
United States dollars	1,134	1,103
	$1,203	$1,182

FUND FOR SPECIAL OPERATIONS
INTER-AMERICAN DEVELOPMENT BANK

APPENDIX II-2

SUMMARY STATEMENT OF LOANS OUTSTANDING – NOTE E

December 31, 2006 and 2005
Expressed in millions of United States dollars

		Currency in which outstanding balance is collectible			
Member in whose territory loans have been made	Outstanding 2006[1]	Non-borrowing country currencies	Borrowing country currencies	Undisbursed	Outstanding 2005
Argentina	$ 109	$ —	$109	$ —	$ 118
Barbados	12	12	—	—	13
Bolivia	955	911	44	495	889
Brazil	281	—	281	4	309
Chile	—	—	—	—	1
Colombia	121	21	100	4	140
Costa Rica	71	65	6	—	81
Dominican Republic	353	338	15	—	366
Ecuador	504	448	56	—	525
El Salvador	450	432	18	—	467
Guatemala	331	284	47	—	344
Guyana	455	454	1	291	402
Haiti	609	599	10	490	550
Honduras	1,264	1,226	38	507	1,167
Jamaica	43	36	7	—	48
Mexico	17	—	17	—	20
Nicaragua	1,060	1,034	26	422	922
Panama	42	36	6	—	50
Paraguay	301	278	23	—	311
Peru	56	23	33	—	66
Suriname	1	—	1	—	1
Trinidad and Tobago	8	—	8	—	9
Uruguay	19	9	10	—	22
Regional	53	51	2	16	52
Total 2006	$7,115	$6,257	$858	$2,229	
Total 2005		$5,936	$937	$2,051	$6,873

(1) Excludes loan participations sold to the Social Progress Trust Fund for a total of $40 million, including $3 million to Bolivia, $8 million to Dominican Republic, $4 million to Ecuador, $3 million to El Salvador, $8 million to Guatemala, $8 million to Honduras, $4 million to Nicaragua, $1 million to Panama and $1 million to Paraguay.

The non-borrowing country currencies in which the outstanding loans balance is collectible are as follows:

Currencies	2006	2005
British pounds sterling	$ 100	$ 92
Canadian dollars	407	418
Danish kroner	36	33
Euro	1,026	930
Japanese yen	340	358
Norwegian kroner	25	24
Swedish kronor	50	44
Swiss francs	71	68
United States dollars	5,131	4,952
	7,186	6,919
Less: HIPC debt relief not delivered yet[2]	929	983
	$6,257	$5,936

(2) Represents the principal component of loans recognized as HIPC debt relief in the Special Purpose Statement of Changes in General Reserve (Deficit), and as a reduction of Loans outstanding in the Special Purpose Statement of Assets, Liabilities and Fund Balance for which debt service relief has not yet been delivered and, accordingly, the related currency of the debt service to be forgiven has not been determined.

FUND FOR SPECIAL OPERATIONS
INTER-AMERICAN DEVELOPMENT BANK

APPENDIX II-3

STATEMENT OF CONTRIBUTION QUOTAS – NOTE G

December 31, 2006 and 2005
Expressed in millions of United States dollars[1]

	Contribution quotas authorized and subscribed				
	Subject to maintenance of value				
Members	Before adjustments	Adjustments[2]	Not subject to maintenance of value	Total 2006	Total 2005
Argentina	$ 402.8	$ 29.5	$ 79.4	$ 511.7	$ 507.7
Austria	11.0	—	9.6	20.6	19.6
Bahamas	8.8	—	1.8	10.6	10.6
Barbados	1.4	—	0.4	1.8	1.8
Belgium	27.1	—	19.7	46.8	44.8
Belize	—	—	7.6	7.6	7.6
Bolivia	32.5	9.7	6.5	48.7	48.7
Brazil	402.8	62.2	79.4	544.4	544.4
Canada	223.8	12.6	80.9	317.3	316.7
Chile	111.4	24.0	22.3	157.7	157.7
Colombia	111.4	20.1	22.2	153.7	153.7
Costa Rica	16.2	4.0	3.2	23.4	23.4
Croatia	3.1	—	2.9	6.0	5.7
Denmark	11.7	—	10.2	21.9	20.8
Dominican Republic	21.7	7.9	4.4	33.9	33.9
Ecuador	21.7	4.2	4.4	30.3	30.3
El Salvador	16.2	2.0	3.2	21.4	21.4
Finland	11.0	—	8.6	19.6	19.0
France	133.4	—	108.5	241.9	230.9
Germany	136.7	—	105.2	241.9	237.7
Guatemala	21.7	6.8	4.3	32.8	32.8
Guyana	7.0	—	1.3	8.3	8.3
Haiti	16.2	2.4	3.2	21.8	21.8
Honduras	16.2	7.1	3.2	26.5	26.5
Israel	10.8	—	8.2	19.0	18.6
Italy	133.4	—	95.9	229.3	219.6
Jamaica	21.7	2.7	4.4	28.8	28.8
Japan	148.8	—	427.7	576.5	580.0
Mexico	259.2	15.0	54.8	329.0	329.0
Netherlands	20.3	—	20.2	40.5	38.4
Nicaragua	16.2	4.8	3.2	24.2	24.2
Norway	11.7	—	8.9	20.6	20.1
Panama	16.2	5.9	3.3	25.4	25.4
Paraguay	16.2	8.5	3.2	27.9	27.9
Peru	54.5	14.3	11.0	79.8	79.8
Portugal	5.0	—	2.8	7.8	7.6
Slovenia	1.8	—	1.6	3.4	3.4
Spain	133.4	—	94.2	227.6	218.1
Suriname	5.3	—	1.0	6.3	6.3
Sweden	23.7	—	17.4	41.1	38.8
Switzerland	38.1	—	29.4	67.5	64.9
Trinidad and Tobago	16.2	1.5	3.2	20.9	20.9
United Kingdom	133.4	—	50.2	183.6	177.6
United States	4,100.0	243.7	495.3	4,839.0	4,839.0
Uruguay	43.5	3.7	8.7	55.9	55.9
Venezuela	250.1	12.1	53.1	315.3	315.3
Total before unallocated amount	7,225.2	504.6	1,990.2	9,720.0	9,665.4
Unallocated[3]	4.0	—	1.4	5.4	5.2
Total 2006	$ 7,229	$ 505	$ 1,992	$ 9,725	
Total 2005	$ 7,228	$ 505	$ 1,937		$ 9,671

(1) Data rounded; detail may not add to subtotals and total because of rounding.
(2) Represent maintenance of value adjustments resulting from the changes in the values of currencies in 1972 and 1973 due to the devaluation of the United States dollar in those years.
(3) Represents the remaining contribution of the former Socialist Federal Republic of Yugoslavia.

INTERMEDIATE FINANCING FACILITY ACCOUNT

REPORT OF INDEPENDENT AUDITORS

Board of Governors
Inter-American Development Bank

We have audited the accompanying balance sheet of the Inter-American Development Bank (Bank)—Intermediate Financing Facility Account as of December 31, 2006 and 2005, and the related statements of changes in fund balance and cash flows for each of the three years in the period ended December 31, 2006. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Bank's Intermediate Financing Facility Account internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Inter-American Development Bank—Intermediate Financing Facility Account as of December 31, 2006 and 2005, and the results of its operations and cash flows for each of the three years in the period ended December 31, 2006, in conformity with United States generally accepted accounting principles.

Ernst + Young LLP

Washington, D.C.
February 6, 2007

INTERMEDIATE FINANCING FACILITY ACCOUNT
INTER-AMERICAN DEVELOPMENT BANK

BALANCE SHEET

Expressed in millions of United States dollars

	December 31,			
	2006		2005	
ASSETS				
Cash and investments				
Cash	$ —		$ 5	
Investments	339	$339	298	$303
Accrued interest on investments		—		1
Total assets		$339		$304
FUND BALANCE				
Fund balance		$339		$304

STATEMENT OF CHANGES IN FUND BALANCE

Expressed in millions of United States dollars

	Years ended December 31,		
	2006	2005	2004
Additions			
Allocations from Fund for Special Operations	**$ 61**	$ 62	$ 73
Income from investments	**17**	9	4
Total additions	**78**	71	77
Deductions			
Interest and principal paid on behalf of Ordinary Capital borrowers	**43**	43	58
Change in fund balance, before translation adjustments	**35**	28	19
Translation adjustments	**—**	(1)	—
Change in fund balance, after translation adjustments	**35**	27	19
Fund balance, beginning of year	**304**	277	258
Fund balance, end of year	**$339**	$304	$277

STATEMENT OF CASH FLOWS

Expressed in millions of United States dollars

	Years ended December 31,		
	2006	2005	2004
Cash flows from operating activities			
Allocations from Fund for Special Operations	**$ 61**	$ 62	$ 73
Income from investments	**5**	9	14
Interest and principal paid on behalf of Ordinary Capital borrowers	**(43)**	(43)	(59)
Net increase in investments	**(28)**	(26)	(29)
Net cash (used in) provided by operating activities	**(5)**	2	(1)
Effect of exchange rate fluctuations on cash	**—**	—	(1)
Net (decrease) increase in Cash	**(5)**	2	(2)
Cash, beginning of year	**5**	3	5
Cash, end of year	**$ —**	$ 5	$ 3

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

INTERMEDIATE FINANCING FACILITY ACCOUNT
INTER-AMERICAN DEVELOPMENT BANK

NOTES TO FINANCIAL STATEMENTS

Note A – Origin
The Inter-American Development Bank (Bank) is an international organization which was established in December 1959. Its purpose is to promote economic and social development in Latin America and the Caribbean, primarily by providing loans and related technical assistance for specific projects and for programs of economic reform. The Agreement Establishing the Inter-American Development Bank (Agreement) provides that its operations be conducted through the Ordinary Capital and the Fund for Special Operations (FSO). In 1983, the Board of Governors of the Bank established the Intermediate Financing Facility Account (IFF) to subsidize part of the interest payments for which certain borrowers are liable on loans from the Ordinary Capital. The IFF receives annual allocations from the FSO, as indicated in Note D.

In making decisions concerning operations of the IFF, the number of votes and percent of voting power for each member country are the same as those applicable for decisions involving the Ordinary Capital, except that the voting authority for decisions to award IFF loan subsidies is determined according to each member country's proportional contribution to the FSO.

Note B – Summary of Significant Accounting Policies
The financial statements are prepared in conformity with United States generally accepted accounting principles (GAAP). The preparation of such financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Translation of currencies
The financial statements are expressed in United States dollars; however, the IFF operations are conducted in various currencies, including the United States dollar. Assets and liabilities denominated in currencies other than the United States dollar are translated at market rates of exchange prevailing at the Balance Sheet dates. Income and expenses in such currencies are translated at market rates of exchange prevailing during each month. The adjustments resulting from the translation of assets and liabilities are shown in the Statement of Changes in Fund Balance as Translation adjustments.[1]

[1]References to captions in the financial statements are identified by the name of the caption beginning with a capital letter every time they appear in the notes to the financial statements.

Investments
Investment securities are recorded using trade-date accounting and are held in a trading portfolio carried at fair value, with changes in fair value included in Income from investments.

Administrative expenses
Administrative expenses of the IFF are paid by the Bank and are allocated between the Ordinary Capital and the FSO, pursuant to an allocation method approved by the Board of Executive Directors.

Fair values of financial instruments
The following methods and assumptions were used in estimating the fair value of the financial instruments:

Cash: The carrying amount reported in the Balance Sheet for cash approximates fair value.

Investments: Fair values for investment securities are based on quoted market prices, where available; otherwise they are based on dealer prices of comparable instruments or discounted cash flows.

Note C – Investments
As part of its overall portfolio management strategy, the Bank invests the IFF resources both directly and indirectly, through an investment pool managed by the Bank, in high quality securities in accordance with established investment guidelines. IFF investments include government, agency, corporate, and bank obligations and asset-backed and mortgage-backed securities with credit ratings ranging from AAA to A+ (short-term securities carry the highest short-term credit ratings).

The Bank limits IFF's activities of investing in securities to a list of authorized dealers and counterparties. Credit limits have been established for each counterparty.

Investment securities held in the trading portfolio are carried at fair value as shown in the Summary Statement of Investments in Appendix III-1. The average return on investments during 2006, including realized and unrealized gains and losses, was 4.99% (2005—3.04%; 2004—1.54%).

Note D – Contributions
The IFF is funded primarily through transfers from the FSO. The IFF is also authorized to receive additional contributions from any member country.

INTERMEDIATE FINANCING FACILITY ACCOUNT
INTER-AMERICAN DEVELOPMENT BANK

NOTES TO FINANCIAL STATEMENTS (continued)

For initial funding purposes, the equivalent of $61 million in convertible currencies of the general reserve of the FSO was transferred to the IFF in 1983. Actual and projected allocations, in accordance with various agreements of the Board of Governors, are shown in the following table (in millions):

Year	Capital increases(1)	HIPC Initiative(2)	Concessional resources agreement(3)	Total
Through 2006	$515	$142	$152	$ 809
2007	30	11	20	61
2008	30	11	20	61
2009	30	11	20	61
2010	30	6	20	56
2011	30	—	20	50
2012 to 2016	—	—	360	360
2017 to 2019	—	—	195	195
Total	$665	$181	$807	$1,653

(1) Under the terms of the Sixth and Seventh General Capital Increases in the Resources of the Bank.

(2) As part of the Heavily Indebted Poor Countries (HIPC) Initiative, the IFF is increasing subsidy payments on Ordinary Capital loans to Bolivia and Guyana. To fund these additional subsidy payments, the Bank is making additional annual transfers in convertible currencies from the FSO's general reserve to the IFF.

(3) Mandated allocations under the Concessional resources agreement approved by the Board of Governors in 1999 amount to $20 million annually from 2000 to 2012 and $15 million in 2013. Additional transfers of approximately $65 million annually from 2012 to 2019 will be necessary to fund the 2000–2008 IFF lending mandated under the Concessional resources agreement. The level of these additional transfers may change as assumptions are revised in future years.

Future allocations are subject to annual approvals by the Board of Governors, and to adjustment for appropriate reasons related to the availability of funding for the IFF. See Note H for possible impact of the proposed New Debt Relief Structure and Concessional Lending Framework on future allocations.

Note E – Translation Adjustments

As indicated in Note B, adjustments resulting from the translation of assets and liabilities into United States dollars are shown as Translation adjustments in the Statement of Changes in Fund Balance. Such adjustments consist of the following for the years ended December 31, 2006, 2005 and 2004 (in millions):

	2006	2005	2004
Cumulative adjustments at January 1,	$43	$44	$44
Translation adjustments	—	(1)	—
Cumulative adjustments at December 31,	$43	$43	$44

Note F – Commitments

The payment by the IFF of part of the interest due from borrowers is contingent on the availability of resources. At December 31, 2006, the amounts disbursed and outstanding and undisbursed, classified by country, under loans on which the IFF would pay part of the interest are as follows (in millions):

Country	Disbursed and outstanding	Undisbursed
Barbados	$ 44	$ —
Bolivia	119	—
Costa Rica	85	—
Dominican Republic	335	42
Ecuador	362	230
El Salvador	327	218
Guatemala	339	184
Guyana	6	—
Jamaica	252	93
Nicaragua	84	—
Panama	81	—
Paraguay	211	149
Suriname	49	34
Trinidad and Tobago	82	—
Uruguay	70	—
Regional	36	—
	$2,482	$950

The interest rate subsidy on certain Ordinary Capital loans is set twice a year by the Board of Executive Directors. The subsidy can be no more than 5% per annum, subject to the effective rate paid by the borrowers being at least 1.5% above the convertible currency FSO average interest rate. For certain loans with increased subsidy under the HIPC I, the effective rate paid by the borrowers can be as low as the convertible currency FSO average interest rate. Up to December 31, 2005, under the Enhanced HIPC Initiative, the IFF subsidized 100% of certain debt service payments (both principal and interest) on Ordinary Capital loans to Nicaragua. It is expected that, over time, the Bank will distribute all of the IFF's resources to subsidize part of the interest payments for which certain Ordinary Capital borrowers are liable.

INTERMEDIATE FINANCING FACILITY ACCOUNT
INTER-AMERICAN DEVELOPMENT BANK

NOTES TO FINANCIAL STATEMENTS (continued)

Note G – Reconciliation of Change in Fund Balance, before Translation Adjustments to Net Cash (Used in) Provided by Operating Activities

A reconciliation of Change in fund balance, before translation adjustments to Net cash (used in) provided by operating activities, as shown on the Statement of Cash Flows, is as follows (in millions):

	Years ended December 31,		
	2006	2005	2004
Change in fund balance, before translation adjustments	$ 35	$ 28	$ 19
Difference between amounts accrued and amounts paid or collected for:			
Income from investments	1	—	(1)
Net unrealized (gain) loss on investments	(13)	—	11
Interest and principal paid on behalf of Ordinary Capital borrowers	—	—	(1)
Net increase in investments	(28)	(26)	(29)
Net cash (used in) provided by operating activities	$ (5)	$ 2	$ (1)
Supplemental disclosure of noncash activities:			
Decrease in investments resulting from exchange rate fluctuations	$ —	$ (1)	$ —

Note H – New Debt Relief Structure and Concessional Lending Framework

In December 2006, the Board of Governors approved a new debt relief structure including one hundred (100) percent relief of eligible FSO debt for Bolivia, Guyana, Haiti, Honduras and Nicaragua, effective January 1, 2007 (Haiti would qualify once it reaches the completion point for the Enhanced HIPC Initiative). Resulting from the approved structure, in January 2007, a Committee of the Board of Governors agreed to submit a proposal to the Board of Governors providing for, inter alia, that countries eligible for IFF subsidies would continue to receive concessional resources for new loans through 2015, in the form of parallel loans (a blending of loans from the FSO and the Ordinary Capital) rather than a reduction in the interest rate billed, and would still receive the reduction in interest rate billed for existing loans, even though allocations from the FSO (as projected in Note D) would not reoccur before 2014. A vote on the proposal is expected in the first quarter of 2007.

INTERMEDIATE FINANCING FACILITY ACCOUNT
INTER-AMERICAN DEVELOPMENT BANK

APPENDIX III-1

SUMMARY STATEMENT OF INVESTMENTS – NOTE C

December 31, 2006 and 2005
Expressed in millions of United States dollars

Investments	2006	2005
Investment Pool	$337	$ —
Obligations of the United States Government and its corporations and agencies	—	39
Obligations of other governments and agencies	—	21
Bank obligations	2	64
Corporate securities	—	13
Asset-backed and mortgage-backed securities	—	161
	$339	$298

The currencies of the above investments are as follows:

Currencies	2006	2005
Euro	$ 2	$ 3
United States dollars	337	295
	$339	$298

GOVERNORS AND ALTERNATE GOVERNORS

Country	Governor	Alternate Governor
ARGENTINA	Felisa Josefina Miceli	Martín P. Redrado
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BAHAMAS	James H. Smith, CBE	Ruth Millar
BARBADOS	Mia Mottley	Grantley Smith
BELGIUM	Didier Reynders	Franciscus Godts
BELIZE	Mark A. Espat	Carla Barnett
BOLIVIA	Luis Hernando Larrazábal Córdova	Luis Alberto Arce Catacora
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CANADA	Peter MacKay	
CHILE	Andrés Velasco	María Olivia Recart Herrera
COLOMBIA	Alberto Carrasquilla Barrera	Carolina Rentería Rodríguez
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CROATIA	Ivan Suker	Ana Hrastovic
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EL SALVADOR	Eduardo Zablah-Touché	William J. Handal
FINLAND	Marjatta Rasi	Anneli Vuorinen
FRANCE	Thierry Breton	Xavier Musca
GERMANY	Karin Kortmann	Rolf Wenzel
GUATEMALA	Hugo Eduardo Beteta Méndez-Ruiz	María Antonieta de Bonilla
GUYANA	Bharrat Jagdeo	Ashni Singh
HAITI	Daniel Dorsainvil	Jean-Max Bellerive
HONDURAS	Rebeca P. Santos	Gabriela Núñez
ISRAEL	Stanley Fischer	Oded Brook
ITALY	Tommaso Padoa-Schioppa	Mario Draghi
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JAPAN	Koji Omi	Toshihiko Fukui
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PORTUGAL	Fernando Teixeira dos Santos	Carlos Costa Pina
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SPAIN	Pedro Solbes Mira	David Vegara Figueras
SURINAME	Humphrey Stanley Hildenberg	Stanley B. Ramsaran
SWEDEN	Jan Knutsson	Stefan Emblad
SWITZERLAND	Jöerg Al. Reding	Roger Denzer
TRINIDAD AND TOBAGO	Camille R. Robinson-Regis	Anthony Bartholomew
UNITED KINGDOM	Hilary Benn	Gareth Thomas
UNITED STATES	Henry Paulson	
URUGUAY	Danilo Astori	Carlos Viera
VENEZUELA	Nelson J. Merentes D.	Jorge Giordani

As of December 31, 2006

EXECUTIVE DIRECTORS AND ALTERNATE EXECUTIVE DIRECTORS

			Number of votes	Percentage of voting power
Charles Bassett, **CANADA** Jill Johnson (Alternate), **CANADA**	**Elected by:** Canada		335,022	4.001
Adina Bastidas, **VENEZUELA** Fernando Eleta Casanovas (Alternate), **PANAMA**	**Elected by**: Panama Venezuela		518,658	6.194
Jerry Christopher Butler, **BAHAMAS** Winston A. Cox (Alternate), **BARBADOS**	**Elected by**: Bahamas Barbados Guyana	Jamaica Trinidad and Tobago	126,574	1.511
Hugo Rafael Cáceres Agüero, **PARAGUAY** Juan E. Notaro (Alternate), **URUGUAY**	**Elected by**: Bolivia Paraguay Uruguay		205,291	2.452
Eugenio Díaz-Bonilla, **ARGENTINA** Martín Bès (Alternate), **ARGENTINA**	**Elected by**: Argentina Haiti		936,545	11.185
Luis Guillermo Echeverri, **COLOMBIA** Gustavo A. Palacio (Alternate), **ECUADOR**	**Elected by**: Colombia Ecuador		295,653	3.531
Agustín García-López, **MEXICO** Roberto B. Saladín (Alternate), **DOMINICAN REPUBLIC**	**Elected by**: Dominican Republic Mexico		627,122	7.489
Giorgio Leccesi, **ITALY** Ina-Marlene Ruthenberg (Alternate), **GERMANY**	**Elected by**: Belgium Germany Israel	Italy Netherlands Switzerland	426,204	5.089
Luis Linde, **SPAIN** Olivier Myard (Alternate), **FRANCE**	**Elected by**: Austria Denmark Finland France	Norway Spain Sweden	400,427	4.783
Héctor E. Morales, **UNITED STATES** Jan E. Boyer (Alternate), **UNITED STATES**	**Appointed by**: United States		2,512,664	30.007
Hugo Noé Pino, **HONDURAS** Nelly Lacayo-Anderson (Alternate), **EL SALVADOR**	**Elected by**: Belize Costa Rica El Salvador	Guatemala Honduras Nicaragua	202,692	2.420
Jaime Quijandría, **PERU** Alejandro Foxley Tapia (Alternate), **CHILE**	**Elected by**: Chile Peru		367,878	4.393
Rogério Studart, **BRAZIL** Arlindo Villaschi (Alternate), **BRAZIL**	**Elected by**: Brazil Suriname		907,766	10.841
Tsuyoshi Takahashi, **JAPAN** Stewart Mills (Alternate), **UNITED KINGDOM**	**Elected by**: Croatia Japan Korea, Republic of	Portugal Slovenia United Kingdom	511,113	6.105
TOTAL			**8,373,609**	**100.00***

Office of Evaluation and Oversight
Stephen A. Quick, Director
Sixto Felipe Aquino, Deputy Director

As of December 31, 2006

* The total may not add up due to rounding.

CHANNELS OF COMMUNICATION AND DEPOSITORIES

Member Country	Channels of Communication	Depositories
ARGENTINA	Ministerio de Economía	Banco Central de la República Argentina
AUSTRIA	Federal Ministry of Finance	Österreichische Nationalbank
BAHAMAS	Ministry of Finance	Central Bank of the Bahamas
BARBADOS	Ministry of Economic Development	Central Bank of Barbados
BELGIUM	Ministère des Finances	Banque Nationale de Belgique
BELIZE	Financial Secretary, Ministry of Finance	Central Bank of Belize
BOLIVIA	Banco Central de Bolivia	Banco Central de Bolivia
BRAZIL	Ministério do Planejamento, Orçamento e Gestão, Secretaria de Assuntos Internacionais—SEAIN	Banco Central do Brasil
CANADA	International Financial Institutions, Multilateral Programs Branch, Canadian International Development Agency	Bank of Canada
CHILE	Ministerio de Hacienda	Banco Central de Chile
COLOMBIA	Ministerio de Hacienda y Crédito Público	Banco de la República
COSTA RICA	Ministerio de Relaciones Exteriores	Banco Central de Costa Rica
CROATIA	Ministry of Finance	National Bank of Croatia
DENMARK	Danish International Development Agency (DANIDA)	Danmarks Nationalbank
DOMINICAN REPUBLIC	Banco Central de la República Dominicana	Banco Central de la República Dominicana
ECUADOR	Ministerio de Economía y Finanzas	Banco Central del Ecuador
EL SALVADOR	Secretaría Técnica de la Presidencia	Banco Central de Reserva de El Salvador
FINLAND	Ministry for Foreign Affairs	Bank of Finland
FRANCE	Ministère de l'économie, des finances et de l'industrie	Banque de France
GERMANY	Federal Ministry for Economic Cooperation and Development	Deutsche Bundesbank
GUATEMALA	Banco de Guatemala	Banco de Guatemala
GUYANA	Ministry of Finance	Bank of Guyana
HAITI	Banque de la République d'Haïti	Banque de la République d'Haïti
HONDURAS	Banco Central de Honduras	Banco Central de Honduras
ISRAEL	Bank of Israel	Bank of Israel
ITALY	Ministry of the Economy and Finance	Banca d'Italia
JAMAICA	Ministry of Finance and Planning	Bank of Jamaica
JAPAN	Ministry of Finance	Bank of Japan
KOREA, REPUBLIC OF	Ministry of Finance and Economy	Bank of Korea
MEXICO	Secretaría de Hacienda y Crédito Público	Banco de México
NETHERLANDS	Ministry of Finance	De Nederlandsche Bank N.V.
NICARAGUA	Ministerio de Hacienda y Crédito Público	Banco Central de Nicaragua
NORWAY	Royal Norwegian Ministry of Foreign Affairs	Bank of Norway
PANAMA	Ministerio de Economía y Finanzas	Banco Nacional de Panamá
PARAGUAY	Banco Central del Paraguay	Banco Central del Paraguay
PERU	Banco Central de Reserva del Perú	Banco Central de Reserva del Perú
PORTUGAL	Ministério das Finanças	Banco de Portugal
SLOVENIA	Ministry of Finance	Bank of Slovenia
SPAIN	Subdirección General de Instituciones Financieras Multilaterales, Ministerio de Economía	Banco de España
SURINAME	Ministry of Finance	Central Bank van Suriname
SWEDEN	Ministry for Foreign Affairs, Department for International Development Co-operation	Sveriges Riksbank
SWITZERLAND	Office fédéral des affaires économiques extérieures	Banque Nationale Suisse
TRINIDAD AND TOBAGO	Central Bank of Trinidad and Tobago	Central Bank of Trinidad and Tobago
UNITED KINGDOM	Department for International Development	Bank of England
UNITED STATES	Treasury Department	Federal Reserve Bank of New York
URUGUAY	Ministerio de Economía y Finanzas	Banco Central del Uruguay
VENEZUELA	Ministerio de Planificación y Desarrollo	Banco Central de Venezuela

As of December 31, 2006

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As of December 31, 2006

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Venezuela

THE INTER-AMERICAN DEVELOPMENT BANK, THE OLDEST AND LARGEST REGIONAL multilateral development institution, was established in 1959 to help accelerate economic and social development in Latin America and the Caribbean. Today, the Bank's membership totals 47 nations, including 26 Latin American and Caribbean countries, the United States, Canada, and 19 nonregional countries.

In carrying out its mission, the Bank has approved $145 billion for projects that represent a total investment of over $335 billion. The Bank's operations cover the entire spectrum of economic and social development, with an emphasis on programs that benefit low-income populations. The IDB lends up to 10 percent of its Ordinary Capital resources directly to the private sector, without government guarantees.

The IDB Group also includes the Inter-American Investment Corporation (IIC), an autonomous affiliate that promotes economic development by financing small and medium-sized private enterprises, and the Multilateral Investment Fund (MIF), which supports micro- and small-enterprise development and market reform.

The financial resources of the Bank consist of the Ordinary Capital account—comprised of subscribed capital, reserves and funds raised through borrowings—and Funds in Administration, comprised of contributions made by member countries. The Bank's charter ensures the position of majority stockholder for the borrowing member countries as a group. The Bank also has a Fund for Special Operations for lending on concessional terms in countries classified as economically less developed. Member country subscriptions to the Bank's Ordinary Capital consist of both paid-in and callable capital. Paid-in capital in the form of cash or notes represents 4.3 percent of total subscriptions. The Bank's debt is AAA rated by the three major rating services in the United States and is accorded equivalent status in the other major capital markets.

The Bank's highest authority is the Board of Governors, on which each member country is represented. The Board of Governors has delegated many of its operational powers to the Board of Executive Directors, which is responsible for the conduct of the Bank's operations.

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