



PE/202/03/3000465

June 23, 2003

Daniele Nouy
Secretary General
Basel Committee Secretariat
Basel Committee on Banking
Supervision
Bank for International Settlements
CH-4002 Basel
Switzerland

Jaime Caruana
Chairman
Basel Committee on Banking
Supervision
and Governor
Banco de España
Alcalá, 50
28014 Madrid
Spain

Dear Secretary General Nouy and Chairman Caruana:

Corporación Andina de Fomento is pleased to have the opportunity to comment on The New Basel Capital Accord consultative document (the "Proposal") issued by the Basel Committee on Banking Supervision (the "Committee") in April 2003.

Corporación Andina de Fomento ("CAF") is a multilateral development bank established in 1968 by an international treaty to foster and promote economic development within the countries of the Andean Community. Its principal shareholders are the Republics of Bolivia, Colombia, Ecuador, Peru and Venezuela. CAF provides project lending and trade financing to public and private sector entities in the Andean Community and the surrounding region. CAF enjoys the privileges and immunities typical of institutions with its supranational status. (For a more detailed description of CAF and its operations, please refer to Annex A to this letter).

In my letter dated November 19, 1999 to Chairman McDonough and Chairman Norgren, I urged the Committee to include multilateral institutions among the entities that would receive risk weightings according to external credit assessments and recommended creating a new category of risk weightings for obligations of multilateral institutions. Accordingly, as stated in my letter dated April 30, 2001 to Secretary General Nouy and Chairman McDonough (the "2001 Letter", attached as Annex B to this letter), CAF welcomes the Proposal's standardized approach for risk weightings that is based on external credit assessments and that would assign a 0% risk weighting to multilateral development banks ("MDBs") that are "highly rated" by the Committee.

Corporación Andina de Fomento

Av. Luis Roche, Torre CAF, Altamira. Caracas. Venezuela. Apartado Postal: Carmelitas 5086.
Teléfono: (58-212) 209.2110 - 209.2030 - Fax: (58-212) 284.2880

CAF continues to believe, however, that MDBs whose long-term obligations are rated A- or better should be entitled to a more favorable rating than banks and corporates with a similar rating—a principle that is applied in the proposal to those MDBs deemed “highly rated” by the Committee. The decision by the Committee not to afford other MDBs a similar preference over banks and corporates results in too great a disparity between the risk weightings assigned to “highly rated” MDBs and other MDBs.

The range between the 0% risk weighting assigned to a “highly rated” MDB and the 50% risk weighting assigned to an A rated MDB, such as CAF, is far greater than the range between the 20% risk weighting for a AAA rated bank or corporate and the 50% risk weighting for an A rated bank or corporate. This disparity is compounded by the fact that, under the proposal, “highly rated” MDBs receive a 0% risk weight for short-term claims, while other MDBs are ineligible for the preferential treatment for short-term claims, set forth in Option 2, accorded to banks with comparable ratings. The principle—recognized in the Proposal—that claims with an original contractual maturity of three months or less are likely to be less risky than a long-term obligation applies just as readily in the MDB context as it does in the private banking sector. Not only does the exclusion of other MDBs from preferential treatment for short-term claims create a disparity between MDBs and similarly situated banks, it further increases the disparity of treatment between “highly rated” MDBs and other MDBs. In addition, the disparity in treatment for short-term claims is inconsistent with the principle—otherwise recognized in the Proposal—that an MDB may be entitled to a more favorable risk weighting than the risk weighting assigned to a bank or corporate carrying a similar credit rating. This principle acknowledges, among other things, the supranational shareholder structure and support that are unique to multilateral institutions.

As stated in the 2001 Letter, CAF proposes that those MDBs with high external credit ratings (AAA to AA- and A+ to A-) that do not otherwise meet the Committee’s eligibility for 0% risk weighting should receive a preferred risk weighting of 20% for long-term claims and 0% for short-term claims rather than the weightings that would be assigned if the Proposal were to be adopted in its current form.

The recognized rating agencies have acknowledged that the multilateral nature of CAF’s ownership structure provides investors greater protection against the risk of default of any single sovereign issuer and accordingly have assigned a significantly higher credit rating to CAF than the sovereign credit ratings of any of its constituent nations, although CAF’s rating is lower than it otherwise would be because a small percentage of its capital is held by investment grade non-sovereign shareholders. For example, Moody’s has recognized that “the special status of the institution as a supranational organization—together with the inherent strength of the institution, as demonstrated by its asset quality, capitalization, and profitability—supports a rating for CAF that exceeds the sovereign ratings of its shareholder countries”. The disparity between CAF’s ratings and those of its borrowers and shareholders signifies the position of the rating agencies that the risk associated with an MDB may be substantially driven

by factors other than the country risk of each of its shareholders and borrowers. Additionally, as specifically noted by S&P, CAF's rating does reflect the country risk embedded in its portfolio and yet, as mentioned, CAF's ratings continue to be significantly higher than those of its constituent nations. The rating agencies have taken a similar approach with respect to other MDBs.

In a paper on risk associated with B loans of MDBs prepared in May 2001 for the Committee (the "B Loan Paper") by the European Bank for Reconstruction and Development (the "EBRD"), the EBRD noted the proven effectiveness of the preferred creditor status of MDBs to mitigate country risk, also referred to as political risk, "including convertibility and transfer risks, breach of contract (by government or quasi-governmental bodies), expropriation, war and civil unrest". Further, and as noted in the B Loan Paper, preferred creditor status has been tested more than once, including during the Latin American debt crisis of the 1980s, the Asia crisis of 1997 and the Russian crisis of 1998. Because of preferred creditor status, among other factors, claims on MDBs should not be assigned the same risk weighting as claims on similarly rated banks and corporates. At a minimum, short term claims of MDBs should not be treated less favorably than those of similarly rated banks and corporates.

In addition to the fact that CAF receives higher ratings from the rating agencies than those of its shareholders, the OECD has assigned CAF an ECA risk score of 2, a score that is much higher than those published for most of its shareholders. The score is assigned to CAF in connection with its operations in support of trade financing. In this capacity, ECAs lend to CAF directly rather than to entities in CAF's shareholder countries. CAF in turn provides credit to those entities.

Under the Proposal, supervisors may use ECA risk scores for risk weighting the claims on sovereigns if such scores are "published by individual ECAs that are recognised by their supervisor, or the consensus risk scores of ECAs participating in the 'Arrangement on Guidelines Officially Supported Export Credits'". Claims on sovereigns receiving an ECA risk score of 2 may be given a risk weighting of 20%. In its August 2000 working paper, "Credit Ratings and Complementary Sources of Credit Quality Information" (the "ECA Paper"), the Committee recognized that "[c]ountry risk evaluation is based on sovereign risk", or political risk, and "involves determining the risk that a loan backed by the importing country's good faith and credit will not be repaid". The ECA risk score assigned to CAF, and the fact that its score is higher than the scores assigned to its sovereign shareholders, reflects the fact that the ECAs may regard MDBs more favorably than they do the related shareholder countries or the corporates of those countries, despite the fact that the credit extended to an MDB may then be extended by that MDB to an entity that an ECA deems substantially less credit-worthy.

In the ECA Paper, the Committee also recognized the strong correlation between ECA risk scores and the ratings assigned by major rating agencies, specifically Moody's, S&P and Thomson. Additionally, of those countries receiving an ECA risk

score of 2, many receive substantially lower ratings from the rating agencies than CAF receives. The use of ECA scores to determine risk weighting for sovereigns but not for MDBs is inconsistent with the aims of the Proposal considering the fact that, for example, a sovereign with ratings of BBB+ to BBB- and an ECA risk score of 5 could receive the same 50% risk weighting as CAF, an entity with an A rating and ECA risk score of 2. In light of these facts, CAF believes that national supervisors should possess the ability to establish risk weights for MDBs as well as sovereigns based on ECA risk scores, to the extent ECA scores are available for MDBs.

With respect to the risk weighting of short-term, issue-specific assessments, the Proposal states that short-term assessments may only be used against banks and corporates. Under the Proposal, the risk weight assigned to a bank's or corporate's issuance with a rating of A-1/P-1 is 20%. CAF respectfully requests that the Committee clarify whether this short-term assessment risk weighting is available to MDBs. If it is not, CAF believes that it should be. Further, CAF believes that the fact that the Committee has determined that 20% is the appropriate risk weighting for issuances with an A-1/P-1 rating provides additional support for its belief that 50% is an overly burdensome risk weight for claims of well rated MDBs.

CAF believes that the foregoing examples of the special consideration afforded to MDBs such as CAF by rating agencies, ECAs and regulatory authorities, coupled with the examples in the 2001 Letter, demonstrate that even MDBs that are not considered "highly rated" are recognizably different from banks and corporates with similar external ratings. At the very least, CAF and similarly situated MDBs should not receive less favorable treatment than equally rated banks in the private sector. Consequently, CAF requests that the Committee continue to evaluate the risk weightings assigned to MDBs with a view to reducing or eliminating the disparity under the Proposal between the risk weightings assigned to (1) "highly rated" MDBs and other MDBs, (2) MDBs and similarly rated banks and corporates and (3) MDBs and sovereigns possessing identical ECA risk scores.

CAF sincerely thanks the Basel Committee for this opportunity to comment on the Proposal. The New Basel Capital Accord is a significant step toward the prudential regulation of international banking, but substantial inequities remain under the Proposal in its present form.

We would welcome an opportunity to discuss these matters with you or any other representatives of the Committee whom you deem appropriate.

Please do not hesitate to contact us in respect of this letter in Caracas, Venezuela at (58) (212) 209-2110.

Sincerely,



L. Enrique Garcia

(Attachments)

cc: Roger W. Ferguson, Jr.,
Vice Chairman
(Federal Reserve System)

Darryll Hendricks
Senior Vice President, Bank Supervision
(Federal Reserve Bank of New York)

José María Roldán Alegre
Director General
(Banco de España)

CORPORACION ANDINA DE FOMENTO

Corporación Andina de Fomento ("CAF") was established in 1968 pursuant to the *Agreement establishing the Corporación Andina de Fomento* (the "Constitutive Agreement"), an international treaty, to foster and promote economic development within the Andean Community countries through the efficient use of financial resources in conjunction with both public and private sector entities. CAF is a multilateral financial institution. Our principal shareholders are the current member countries of the Andean Community — the Republics of Bolivia, Colombia, Ecuador, Peru and the Bolivarian Republic of Venezuela (collectively accounting for 94.4% of paid-in capital). Argentina, Brazil, Chile, Mexico, Panama, Paraguay, Spain, Trinidad and Tobago and Uruguay are non-regional shareholders (collectively accounting for 5.5% of paid-in capital). Shares are also held by 21 financial institutions from within the Andean Community countries (collectively accounting for 0.1% of paid-in capital). CAF commenced operations in 1970. Our headquarters is in Caracas, Venezuela, and we have regional offices in the capital cities of each of the five Andean Community countries.

Our objective is to support sustainable development and economic integration within the Andean Community countries by helping the Andean Community countries make their economies diversified, competitive and more responsive to social needs.

As an international treaty organization, CAF is a legal entity under public international law. CAF has its own legal personality, which permits it to enter into contracts, acquire and dispose of property and take legal action. The treaty establishing CAF has been ratified by the legislature in each of the Andean Community countries. CAF has been granted the following immunities and privileges:

- (1) immunity from expropriation, search, requisition, confiscation, seizure, sequestration, attachment, retention or any other form of forceful seizure by reason of executive or administrative action by any of the Andean Community countries and immunity from enforcement of judicial proceedings by any party prior to final judgment;
- (2) free convertibility and transferability of our assets;
- (3) exemption from all taxes and tariffs on income, properties or assets, and from any liability involving payment, withholding or collection of any taxes; and
- (4) exemption from any restrictions, regulations, controls or moratoria with respect to our property or assets.

CAF's primary operations are project and corporate lending and trade finance. Within the Andean community countries, CAF extends medium-term and long-term loans to finance both public and private sector projects. Also, CAF provides credit

lines to financial institutions in the Andean Community countries to enable those institutions to finance projects. Through trade finance, CAF endeavors to strengthen trade and assist companies located in the Andean Community countries in their efforts to access world markets.

The Constitutive Agreement delegates to our Board of Directors, the power to establish and direct our financial, credit and economic policies. A formal statement of our financial and operational policies, the *Políticas de Gestión* ("Operational Policies"), has been adopted by the Board of Directors. The Operational Policies provide our management with guidance as to significant financial and operational issues.

CAF raises funds for operations both within and outside the Andean Community countries. CAF's strategy with respect to funding, to the extent possible under prevailing market conditions, is to match the maturities of CAF's liabilities to the maturities of its loan portfolio. CAF is an active issuer in the international capital markets. Since 1993, CAF has issued debt securities on various markets and in various currencies worth over US\$5.8 billion in aggregate.

April 30, 2001

PE-125-0535/01

William J. McDonough
Chairman
Basel Committee on Banking
Supervision
and President
Federal Reserve Bank of New York
33 Liberty Street
New York, NY 10045

Daniele Nouy
Secretary General
Basel Committee Secretariat
Basel Committee on Banking
Supervision
Bank for International Settlements
CH-4002 Basel, Switzerland

Dear Chairman McDonough and Secretary General Nouy:

Corporación Andina de Fomento is pleased to have the opportunity to comment on The New Basel Capital Accord consultative document (the "Proposal") issued by the Basel Committee on Banking Supervision in January 2001.

Corporación Andina de Fomento ("CAF") is a multilateral development bank established in 1968 by an international treaty to foster and promote economic development within the countries of the Andean Community. Its principal shareholders are the Republics of Bolivia, Colombia, Ecuador, Peru and Venezuela. CAF provides project and corporate lending and trade financing to public and private sector entities in the Andean Community and the surrounding region. CAF enjoys the privileges and immunities typical of institutions with its supranational status. (For a more detailed description of CAF and its operations, please refer to Annex A to this letter)

In my letter dated November 19, 1999, to Chairman McDonough and Chairman Norgren, I urged the Committee to include multilateral institutions among the entities that would receive risk weightings according to external credit assessments and recommended creating a new category of risk weightings for obligations of multilateral institutions. Accordingly, CAF welcomes the Proposal's new standardized approach for risk weightings that is based on external credit assessments and that would assign a 0%

Corporación Andina de Fomento

Av. Luis Roche, Torre CAF, Altamira. Caracas, Venezuela. Apartados Postales: Carmelitas 5086 y Altamira 69011 - 69012.

Teléfono: (582) 209.2111 - Fax: (582) 284.5754

risk weighting to multilateral development banks ("MDBs") that are "highly rated" by the Committee.

The Proposal recognizes the principle that an MDB may be entitled to a more favorable risk weighting than the risk weighting that would be assigned to a bank or corporate entity carrying a similar credit rating from a recognized credit rating agency, in part because of the supranational shareholder structure and support that is unique to multilateral institutions. The Proposal currently provides that an MDB, a majority of whose long-term securities are rated AAA, would be entitled to a 0% risk weighting if the Committee determines it to be "highly rated", whereas the risk weighting of claims on a bank or corporate with a similar external credit rating would be 20%.

CAF believes that this same principle should be extended to MDBs whose long-term securities are rated A- or better and that their supranational structure and support should entitle them to a more favorable risk weighting than banks and corporates with a similar securities rating. Under the Proposal as currently drafted, MDBs that do not satisfy the Basel Committee's criteria for 0% risk weighting are assigned the same risk weightings as banks and corporates with similar external credit ratings. This results in a significant risk weighting disparity among MDBs that does not apply to any other category of issuers under the Proposal, i.e., the range between the 0% risk weighting assigned to a AAA "highly rated" MDB and the 50% risk weighting assigned to an A-rated MDB, such as CAF, is far greater than the range between the 20% risk weighting for a AAA rated bank or corporate and the 50% risk weighting for a A- rated bank or corporate.

In light of the 0% risk weighting assigned to many of the MDBs with which CAF competes in the capital markets for funds, the 50% risk weighting assigned to CAF's obligations and the 20% risk weighting assigned to its short-term obligations would unduly adversely affect CAF's cost of funds and, under certain market conditions, could adversely affect its ability to raise funds in the international capital markets. An MDB, such as CAF, whose long-term securities are rated A and to which a 50% risk weighting is assigned under the Proposal, may find it more difficult to compete with a "highly rated" MDB assigned a 0% risk weighting than is currently the case. CAF believes this disparity is too great and that it can and should be reduced as the Basel Committee continues to refine the new capital adequacy framework.

Specifically, CAF proposes that those MDBs with high external credit ratings (AAA to AA- and A+ to A-) that do not otherwise meet the Basel Committee's standard for 0% risk weighting should receive a preferred risk weighting of 20% for long-term claims and 0% for short-term claims rather than the levels that would prevail under the Proposal.

While CAF acknowledges that the ratings of its member countries may not at the present time satisfy the Basel Committee that CAF should receive 0% risk weighting, CAF respectively requests that the Basel Committee note CAF's supranational and preferred creditor status and superior credit quality as recognized by external credit assessment institutions through the assignment of strong investment grade ratings and by G-10 bank regulatory authorities through exemptions from country risk provisioning requirements.

For example, although CAF's rating is limited by the fact that virtually none of its capital is held by investment grade shareholders, the recognized rating agencies have acknowledged that the multilateral nature of CAF's ownership structure provides investors greater protection against the default risk of any single sovereign issuer and have assigned a significantly higher credit rating to CAF than the sovereign ceilings of any of its constituent nations. Moody's has recognized that "the special status of the institution as a supranational organization - together with the inherent strength of the institution, as demonstrated by its asset quality, capitalization, and profitability - supports a rating for CAF that exceeds the sovereign ratings of its shareholder countries." The rating agencies have taken a similar approach with respect to other multilateral development banks.

Various G-10 bank regulatory authorities have also recognized CAF's supranational status as well as its superior credit quality. The bank regulatory authorities of Belgium, France, Spain, Switzerland, the United Kingdom and the United States have exempted bank loans to CAF from the country risk provisioning requirements applicable from time to time to bank loans to entities incorporated in CAF's member states. The bank regulatory authorities of Belgium, France and The Netherlands have also extended this provisioning exemption to co-financing loans for which CAF remains the lender of record, thereby providing default protection to the syndicate participants.

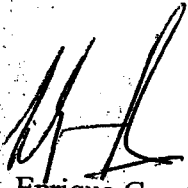
In conclusion, CAF believes that the foregoing examples of the special consideration afforded to MDBs such as CAF by rating agencies and regulatory authorities demonstrate that even MDBs that are not deemed to be "highly rated" are recognized as different from banks and corporates with similar external securities ratings. Consequently, CAF requests that the Committee continue to evaluate the weightings assigned to MDBs with a view to reducing or eliminating the disparity under the Proposal between the risk weightings assigned to "highly rated" MDBs and other MDBs.

CAF sincerely thanks the Basel Committee for this opportunity to comment on the Proposal and to inform the Committee of substantial inequities under the 1988 Accord in its present form.

We would welcome any opportunity to discuss these matters with you or any other representatives of the Basel Committee whom you deem appropriate.

Please do not hesitate to contact us in respect of this letter, or the themes discussed herein, in Caracas, Venezuela at (58) (212) 209-2110.

Sincerely,



L. Enrique García
President & CEO

(Attachments)

cc: Roger Cole
Board of Governors of the Federal Reserve System

Darryll Hendricks
Federal Reserve Bank of New York

CORPORACION ANDINA DE FOMENTO

Corporación Andina de Fomento ("CAF") was established in 1968 pursuant to the Constitutive Agreement, an international treaty, to foster and promote economic development within the Andean Community countries by the efficient use of financial resources in conjunction with both public and private sector entities. CAF is a supranational financial institution. Our principal shareholders are the current member countries of the Andean Community – the Republics of Bolivia, Colombia, Ecuador, Peru and Venezuela (collectively accounting for 95.8% of paid-in capital). Brazil, Chile, Mexico, Panama, Paraguay and Trinidad and Tobago are non-regional shareholders (collectively accounting for 4.1% of paid-in capital). Shares are also held by 22 financial institutions from within the Andean Community countries (collectively accounting for 0.1% of paid-in capital). CAF commenced operations in 1970. Our headquarters is in Caracas, Venezuela, and we have regional offices in the capital cities of each of the five Andean Community countries.

Our objective is to support sustainable development and economic integration within the Andean Community countries by assisting the Andean Community countries in making their economies diversified, competitive and more responsive to social needs.

As a supranational institution, CAF is a legal entity under public international law, created by an international treaty, CAF has its own legal personality, which permits us to enter into contracts, acquire and dispose of property and take legal action. Our Constitutive Agreement has been ratified by the legislature in each of the Andean Community countries, where we have been granted the following immunities and privileges:

- (1) immunity from expropriation, search, requisition, confiscation, seizure, sequestration, attachment, retention or any other form of forceful seizure by reason of executive or administrative action by any of the Andean Community countries and immunity from enforcement of judicial proceedings by any party prior to final judgment;
- (2) free convertibility and transferability of our assets;
- (3) exemption from all taxes and tariffs on income, properties or assets, and from any liability involving payment, withholding or collection of any taxes; and
- (4) exemption from any restrictions, regulations, controls or moratoria with respect to our property or assets.

Our primary operations are project and corporate lending and trade finance. Within the Andean community countries, we provide financing for public and private sector projects and, through trade finance, endeavor to strengthen trade and assist companies located in the Andean Community countries in their efforts to access world markets. Project loans are specific-purpose loans to public entities or corporations, and the term "project loan" generally does not denote limited-recourse financing.

The Constitutive Agreement delegates to our Board of Directors, the power to establish and direct our financial, credit and economic policies. A formal statement of our financial and operational policies, the *Políticas de Gestión* ("Operational Policies"), has been adopted by the Board of Directors. The Operational Policies provide our management with guidance as to significant financial and operational issues.

CAF raises funds for operations both within and outside the Andean Community countries. Our strategy with respect to funding and borrowing has been to obtain long-term and medium-term funds for project and corporate loans and short-term funds for trade loans. CAF is an active issuer in the international capital markets. Since 1993, CAF has issued debt securities on various markets and in various currencies worth over US\$4.1 billion in aggregate.