Translation of financial statements originally issued in Spanish

Panama Canal Authority

Independent Auditors' Report

Financial statements
September 30, 2009

Deloitte – Panama

Panama Canal Authority

Independent Auditors' Report and Financial Statements September 30, 2009

Content	**Pages**

Deloitte.

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TRANSLATION OF A REPORT ORIGINALLY ISSUED IN SPANISH

INDEPENDENT AUDITORS' REPORT

To the Board of Directors of the Panama Canal Authority

Report on the financial statements

We have audited the accompanying financial statements of the Panama Canal Authority, which comprise the balance sheet as at September 30, 2009, and the statements of income, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies applied and other explanatory notes.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable according to the circumstances.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity' s internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Panama Canal Authority as at September 30, 2009, and the results from its operations and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

(Signed by Deloitte)

December 17, 2009
Panama, Republic of Panama

Panama Canal Authority

Balance sheet
September 30, 2009
(In thousands of balboas)

	Notes	2009	2008
Assets			
Non-current assets:			
Properties, plant and equipment, net	4, 16	2,679,067	2,438,710
Current assets:			
Cash, cash equivalents, and bank deposits	5	2,507,390	1,653,148
Investment securities (held to maturity)	6, 19	-	470,426
Hedge instrument	7	57,457	-
Accounts receivable	8	33,614	35,192
Inventories, net	9	49,653	39,861
Accrued interest receivable and other assets		7,604	22,379
Total current assets		2,655,718	2,221,006
Total assets		5,334,785	4,659,716
Equity and liabilities			
Equity:			
Contributed capital	16	1,904,968	1,904,968
Retained earnings:			
Reserved	10	2,732,554	2,159,761
Unappropriated	11	434,120	343,852
Adjustment for hedge instrument valuation	7	6,478	-
Total equity		5,078,120	4,408,581
Current liabilities:			
Accounts payable	12	125,903	119,358
Provision for marine accident claims	13	32,368	27,474
Accrued salaries and vacation payable		90,755	90,535
Other liabilities		7,639	13,768
Total current liabilities		256,665	251,135
Total equity and liabilities		5,334,785	4,659,716

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

Panama Canal Authority

Income statement
For the year ended September 30, 2009
(In thousands of balboas)

	Notes	2009	2008
Revenues:			
Toll revenues		1,438,175	1,317,475
Other Canal transit services		379,224	428,103
		1,817,399	1,745,578
Other revenues:			
Electric power sales		79,463	142,895
Potable water sales		20,247	19,709
Interest income		32,789	70,875
Miscellaneous	17	12,138	27,988
Total other revenues		144,637	261,467
Total revenues		1,962,036	2,007,045
Expenses:			
Salaries and wages		359,185	354,959
Employee benefits		49,661	49,402
Materials and supplies		51,596	41,407
Fuel		61,001	100,287
Transportation and allowances		1,333	1,366
Contracted services and fees		40,889	41,030
Insurance		11,141	10,020
Provision for marine accidents	13	7,410	642
Provision for obsolete inventory	9	590	772
Other expenses		14,238	8,998
		597,044	608,883
Capitalized labor and materials	14	(61,635)	(55,711)
Total expenses		535,409	553,172
Income before fees and depreciation		1,426,627	1,453,873
Fees per net ton	12	(344,320)	(355,034)
Panamanian Treasury (Tesoro Nacional) - public service fees		(1,964)	(1,874)
Depreciation	4	(73,430)	(68,503)
Net income	15	1,006,913	1,028,462

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

Panama Canal Authority

Statement of changes in equity
For the year ended September 30, 2009
(In thousands of balboas)

	Notes	Contributed Capital	Retained Earnings Reserved	Retained Earnings Unappropriated	Adjustment for hedge instrument valuation	Total equity
Balance as of September 30, 2007		1,904,968	1,475,151	486,414	-	3,866,533
Transfer to Panamanian Treasury	11	-	-	(486,414)	-	(486,414)
Net income		-	-	1,028,462	-	1,028,462
Contributions to the investment program	10	-	579,032	(579,032)	-	-
Increase in equity reserves	10	-	105,578	(105,578)	-	-
Balance as of September 30, 2008		1,904,968	2,159,761	343,852	-	4,408,581
Transfer to Panamanian Treasury	11	-	-	(343,852)	-	(343,852)
Net income		-	-	1,006,913	-	1,006,913
Cash flow hedge	7	-	-	-	6,478	6,478
Contributions to the investment program	10	-	507,868	(507,868)	-	-
Increase in equity reserves	10	-	64,925	(64,925)	-	-
Balance as of September 30, 2009		1,904,968	2,732,554	434,120	6,478	5,078,120

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

Panama Canal Authority

Statement of cash flows
For the year ended September 30, 2009
(In thousands of balboas)

	Notes	2009	2008
Cash flows from operating activities:			
Net income		1,006,913	1,028,462
Adjustments for:			
Depreciation	4	71,990	66,180
Loss on disposal of fixed asset		2,292	1,114
Provision for obsolete inventory	9	590	772
Provision for marine accidents	13	7,410	642
Severance payable	17	-	(10,000)
Changes in operating assets and liabilities:			
Accounts receivable		1,578	1,920
Inventories		(10,382)	(5,265)
Accrued interest receivable and other assets		14,775	3,772
Current liabilities		(1,880)	47,157
Net cash provided by operating activities		1,093,286	1,134,754
Cash flows from investing activities:			
Net increase of fixed asset		(314,639)	(266,311)
Net decrease (increase) in investments	6	470,426	(135,264)
Net increase in time deposits, over 90 days		(892,675)	(238,586)
Hedge instrument	7	(50,979)	-
Net cash used in investing activities		(787,867)	(640,161)
Cash flows from financing activities:			
Transfer to Panamanian Treasury	11	(343,852)	(486,414)
Net (decrease) increase in cash and cash equivalents		(38,433)	8,179
Cash and cash equivalents at beginning of the year		250,658	242,479
Cash and cash equivalents at end of the year	5	212,225	250,658
Investing activities that did not represent cash outflows			
Fixed assets - capitalized depreciation	4, 14	(1,440)	(2,323)

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

1. General Information

The Panama Canal Authority (PCA) is an autonomous agency of the Government of Panama, established in conformity with Article 316 of the Political Constitution of the Republic of Panama. The PCA is responsible for the administration, operation, conservation, maintenance, modernization, and other related activities of the Panama Canal (the Canal), that are necessary to ensure the safe, uninterrupted, efficient and profitable operation of the Canal in accordance with the constitutional and legal regulations in effect. The PCA has its own patrimony and the right to manage it. The PCA was organized on June 11, 1997 under Law No.19 (Organic Law).

The PCA, in coordination with government entities designated by law, is also responsible for the management, maintenance, use and conservation of the water resources of the Canal watershed, including lakes and their tributary streams.

With the expiration of the 1977 Torrijos-Carter Treaty at noon on December 31, 1999, the Panama Canal reverted to the Republic of Panama free of debts and liens, becoming an inalienable patrimony of the Republic of Panama, open to the peaceful and uninterrupted passage of vessels of all nations and whose use will be subject to the requirements and conditions established by the Political Constitution of Panama, the Organic Law of the PCA, and its management.

As of September 30, 2009, the PCA had a total of 9,671 (2008: 9,447) employees, of which 8,147 (2008: 7,797) were permanent and 1,524 (2008: 1,650) were temporary.

The main PCA offices are located at the Administration Building #101, Balboa, Republic of Panama.

The financial statements of the Panama Canal Authority for the period ended as of September 30, 2009, were approved by the Board of Directors and authorized for their issuance on December 17, 2009.

2. Adoption of New and Revised International Financial Reporting Standards

At the date of these financial statements, the following standards and interpretations were issued but not yet in effect:

Standard and Interpretation	Effective Date
IAS 1 (Revised) - Presentation of Financial Statements	January 1, 2009
IFRS 8 - Operating segments, replaces IAS 14, Segment reporting	January 1, 2009
IAS 23 (Revised) - Borrowing costs	January 1, 2009
IAS 32 (Amendment) Financial Instruments	January 1, 2009
IFRIC 14 - The limit on a defined benefit asset, minimum funding requirements and their interaction	January 1, 2009

The Administration considers that the adoption of these standards and interpretations applicable to future periods, would not have an important effect in PCA's financial statements.

3. Significant accounting policies

3.1. Statement of compliance

PCA's financial statements, including the comparatives figures, have been prepared in accordance with International Financial Reporting Standards, issued by the International Accounting Standard Board ("IASB") and the interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC) of the IASB.

3.2. Basis of presentation

The financial statements have been prepared under the historical cost basis, except for the recognition of changes in foreign currency of hedge instruments. PCA applied accounting policies consistent with those applied in the prior year.

3.3. Use of estimates

These financial statements are prepared in conformity with IFRS which requires management to make estimates and assumptions. These assumptions 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. Future actual results could differ from those estimates. Significant estimates for these financial statements include the provision for marine accident claims, provision for obsolete inventory of materials and supplies, and the determination of the useful life of fixed assets.

3.4. Properties, plant, and equipment

Items of properties, plant, and equipment with a value of B/.5 or more are recorded at cost. The cost of items that are not capitalized or under B/.5 is expensed as incurred.

Depreciation is calculated using the straight-line method over the following estimated useful lives:

Buildings	25 - 75 years
Structures	5 - 100 years
Equipment	3 - 75 years

The assets' useful lives are reviewed periodically to ensure that the depreciation period is consistent with the expected economic benefit of the components of properties, plant, and equipment.

The gain or loss resulting from the retirement or disposal of an asset is the difference between the net proceeds and the net book value of the asset. The gain or loss is reflected in the statement of income when incurred, except for buildings and properties that were received from the Government of Panama, which are charged against equity when they are demolished or returned to the Government of Panama once it is determined they have no operating use for the PCA.

Maintenance and repairs are expensed as incurred, while major improvements are capitalized. Dredging costs incurred for recurrent maintenance of the waterway, as a result of landslides and erosion, are expensed. Dredging costs for substantial improvements to the waterway are capitalized and depreciated over their estimated useful lives.

Construction in progress represents plant and properties under construction and includes the cost construction and other direct costs. These assets are depreciated when completed and placed in operation.

3.5. Impairment of long term assets

Assets that are subject to amortization are reviewed annually to identify any impairment losses, whenever events or changes in circumstances indicate that the carrying amounts may not be recoverable. An impairment loss is recognized for the amount by which an asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's net selling price and its value in use.

3.6. Financial instruments

The financial assets and liabilities are recognized in the balance sheet of the PCA when they become a contractual obligation of the instrument.

- ***Cash, cash equivalents and bank deposits*** - Consist of cash on hand, deposits in current and saving accounts, and time deposits, free of liens and with original maturity dates of less than 90 days or over 90 days not exceeding one year.

- ***Accounts receivable* -** Accounts receivable are recorded at their face value.

- ***Classification of financial assets and liabilities into current or non-*current -** Financial assets and liabilities are classified according to their maturity date on the balance sheet. Current assets and liabilities are those with a maturity date that is less than or equal to twelve months. Non-current assets and liabilities are those with a maturity date greater than twelve months.

- ***Write-off of financial assets*** - Financial assets are written off only when the contractual rights to receive cash flows have expired; or where in the transfer of financial assets, substantially all the risks and benefits inherent in ownership of the asset were transferred to another entity. If the entity does not transfer and does not retain substantially all the risks and benefits of ownership and continues to control the transferred asset, the entity recognizes its retained interest in the asset as well as a liability for the amount it may have to pay. If the entity retains substantially all the risks and benefits of ownership of the financial asset transferred, the entity continues to recognize the financial asset and also recognizes a liability secured by the amount received.

- ***Impairment of financial assets* -** Financial assets are assessed at the end of each reporting period to determine whether there is evidence of impairment. A financial asset is impaired if there is evidence that as a result of one or more events that occurred after the initial recognition of the asset there has been an impact on the estimated future cash flows of the financial asset.

- ***Accounts payable*** - Accounts payable do not earn interests explicitly and are recorded at their face value.

- ***Write-off of financial liabilities*** - The entity removes financial liabilities when, and only when, the entity's obligations are discharged, cancelled or expired.

3.7. Investment securities

Purchases of investments are recognized on the settlement date, the date on which PCA pays and receives the asset.

Investment securities are acquired with the intention to be held to maturity and are recorded at amortized cost. Amortized cost is the initial cost of the investment, adjusted by the cumulative amortization of any discount or premium on acquisition. The amortization of the discount or premium is recognized as an increase or decrease of interest income in the statement of income.

3.8. Hedge instrument

The entity recognizes at fair value all assets or liabilities arising from operations with derivative financial instruments on the balance sheet, independently of the purpose for holding them. Fair value is determined based on quoted market prices and, when not traded in an active market, is determined by using valuation techniques accepted in the financial sector.

When hedging instruments are contracted with the aim of hedging risks and comply with all hedging requirements, their designation is documented at the beginning of the hedging relationship, describing the objective, characteristics, accounting recognition, and how effectiveness will be measured, as applicable to that operation.

Hedging instruments designated as hedges recognize changes in valuation according to the type of hedging involved: (1) for fair value hedges, fluctuations in the fair value of the derivative, as well as fluctuations of the hedged item are valued at fair value and are recognized in profit and loss; (2) for cash flow hedges, the effective portion is temporarily recognized in equity as comprehensive income and recycled in the income statement when the hedge item affects profit or loss; the ineffective portion is recognized immediately in profit and loss.

The entity shall discontinue the hedge accounting when the derivative expires, is sold, terminated or exercised, when the hedging instrument does not achieve a high effectiveness to compensate for the changes in fair value or cash flows of the hedged item, or when the entity decides to cancel the hedge designation.

In cash flow hedges, when hedge accounting is discontinued, the amounts recorded in equity as comprehensive income shall remain in equity until the forecasted transaction or firm commitment affect profit and loss. When a forecasted transaction or firm commitment is no longer expected to occur, the cumulative gains or losses that were reported in equity as comprehensive income are immediately transferred to the income statement. If the hedging of a forecasted transaction had been shown as effective and later does not comply with the effectiveness test, the accumulated effects in the comprehensive income equity account are carried proportionally to the income statement to the extent that the forecasted asset or liability affects the profit and loss.

All investments, deposits and/or certificates of deposits of the PCA, are denominated in the currency of the United States of America, or in other currencies exclusively for payment to vendors for contracts awarded in such currencies, without the intention of speculating and with the sole purpose of mitigating the foreign currency exchange risk. Topics related to foreign exchange rate volatility are documented with the purpose of mitigating the risk related to payments of the awarded contracts. Deposits are renewed for remaining balances as periodic payments are made and interests are generated. Interests are considered part of the hedge, and are capitalized to the deposit until the entire contract is paid. To determine the prospective effectiveness, a historic correlation is made between the variations in the exchange rate of the deposit with the variations experienced by the commitment of the purchase contracted. The method used to determine the retrospective effectiveness is the dollar off-set method for cumulative changes.

3.9. Inventories

Inventories of materials, operating supplies, and fuel are presented at the lower of cost and net realizable value. Inventories are valued based on the average cost method according to the valuation of suppliers which after the allowance for obsolescence of materials and supplies inventory, does not exceed the realizable value.

3.10. Allowance for obsolete materials and supplies

The inventory of supplies and materials is evaluated annually to determine the adequacy of stock levels. If determined to be excessive, these should be reduced due to obsolescence, impairment, diminishment of quality, slow turnover or as a result of not being useful for the operation and functioning of the Canal.

If any inventory item of supplies and materials complies with the previously mentioned characteristics, the allowance is adjusted to its reasonable value to recognize the probable loss.

3.11. Revenue recognition

Revenues are recognized when it is probable that future economic benefits will flow to the PCA and those benefits can be measured reliably. The following specific criteria have to be complied before revenues are recognized:

Toll revenue
The toll revenue is recognized once vessels complete their transits through the Canal.

Electric power sales revenue
The PCA has the capacity to produce both hydropower and thermal power to generate electricity needed for canal operations. Excess production is sold in the open market through contracts with distributors of electricity and other third parties.

Potable water sales revenue
The PCA has the capacity to produce and supply potable water for consumption within its facilities. Surplus production is sold to the National Institute of Pipelines and Sewerage (Instituto de Acueductos y Alcantarillados Nacionales).

Services rendered
Revenues from other services are recognized when services are rendered.

Interest
Interest income on bank deposits and investments are recognized as accrued.

3.12. Embedded derivatives

Derivatives may be embedded in other contractual agreement (a "host contract"). The entity accounts for the embedded derivative separately when the host contract is not carried at fair value by means of profit or loss, and if because of the characteristics of the embedded derivative it is not closely related to the host contract. Separated embedded derivatives are accounted for depending on their classification and are presented on the balance sheet together with the host contract.

3.13. Monetary unit

The PCA maintains its accounting records and financial statements in balboas (B/.). The balboa, monetary unit of the Republic of Panama, is at par and has free exchange with the U.S. dollar. The Republic of Panama does not issue paper money and in its place utilizes the U.S. dollar as legal currency.

Assets and liabilities denominated in foreign currencies are converted to balboas (B/.), at the exchange rate prevailing at the end of the period.

3.14. Critical judgment in the application of accounting policies

Fixed assets:

To determine the useful life of fixed assets, a catalog of property, plant, and equipment units is used. This catalog is an internal guide that identifies the basis to determine the elements of a fixed asset, based upon the criteria established in the International Financial Reporting Standards.

This catalog details all the assets according to function and useful life, within the main objective of unifying the criteria used in the classification of capital assets and the estimation of depreciation expense.

Marine accident claims:

The PCA records a provision for marine accidents as soon as a known probable economic obligation is derived from any particular incident. Such provision includes an estimate of costs for repairs, dry dock, damages to cargo and inspection, among others. These elements constitute the basis to record the initial liability which is updated based on inspections or presentation of properly supported claims.

The PCA will make payments for claims that are properly supported and accepted by the PCA during the administrative or judicial stage or in conformity with the Organic Law, Article 69. The PCA will also make payments in compliance with final rulings of the Maritime Tribunal, in cases where the PCA may be liable.

(In thousands of balboas)

4. Properties, plant and equipment, net

Properties, plant and equipment are as follows:

	September 30, 2009			
	Beginning Balance	Additions	Decreases	Ending Balance
Assets				
Land	1,022,767	-	-	1,022,767
Buildings	92,494	375	(441)	92,428
Structures	701,728	47,856	(1,297)	748,287
Equipment	868,582	28,251	(15,972)	880,861
Constructions in progress	273,635	240,753	-	514,388
	2,959,206	317,235	(17,710)	3,258,731
Accumulated depreciation				
Buildings	28,912	2,953	(7)	31,858
Structures	153,610	25,553	(120)	179,043
Equipment	337,974	44,924	(14,135)	368,763
	520,496	73,430	(14,262)	579,664
Net value	2,438,710	243,805	(3,448)	2,679,067

(In thousands of balboas)

	September 30, 2008			
	Beginning Balance	**Additions**	**Decreases**	**Ending Balance**
Assets				
Land	1,022,581	186	-	1,022,767
Buildings	87,705	4,813	(24)	92,494
Structures	602,784	98,945	(1)	701,728
Equipment	786,324	85,330	(3,072)	868,582
Constructions in progress	194,275	79,360	-	273,635
	2,693,669	268,634	(3,097)	2,959,206
Accumulated depreciation				
Buildings	26,186	2,750	(24)	28,912
Structures	130,614	22,997	(1)	153,610
Equipment	297,176	42,756	(1,958)	337,974
	453,976	68,503	(1,983)	520,496
Net value	2,239,693	200,131	(1,114)	2,438,710

The PCA recorded losses as a result of retirements or disposals of assets of B/.2,292 (2008: B/.1,114). During 2009, the main assets that were retired included a barge tie up station, hydraulic excavator with its spare parts, vehicles and printing equipment. During 2008, the main assets that were retired included diesel motors, communication equipment, elevators, vehicular equipment, pumps, containers, film processors, surveillance and intrusion detection systems.

A portion of the depreciation of B/.1,440 (2008: B/.2,323) corresponding to equipment utilized in investment projects was capitalized as properties, plant and equipment during the period (See note 14).

(In thousands of balboas)

At the end of fiscal year 2009, constructions in progress included Investment Program - Other totaling B/.151,989 (2008: B/.160,002) and the Investment Program - Canal Expansion totaling B/.362,399 (2008: B/.113,633). The latter includes commissions and other costs of financing totaling B/.14,930 during fiscal year 2009 (2008: B/.-).

5. Cash, cash equivalents and bank deposits

Cash, cash equivalents and bank deposits are comprised of the following:

	2009	**2008**
Cash on hand	49	33
Deposits in current accounts	27,129	22,455
Deposits in saving accounts	120,046	64
Time deposits with original maturities under 90 days	65,001	228,106
Total cash and cash equivalents	212,225	250,658
Time deposits with original maturities over 90 days not exceeding one year	2,295,165	1,402,490
Total bank deposits	2,507,390	1,653,148

Article 44 of the Organic Law states that PCA's funds may be placed in short-term investment grade instruments and may not be used to buy other types of financial investment instruments issued by Panamanian or foreign public or private entities, or to grant loans to such entities or to the Panamanian Government. All PCA investments in time deposits are placed in investment grade banks.

(In thousands of balboas)

6. Investment securities (held to maturity)

During fiscal year 2008, investments consisted of bonds which were acquired with the intention of being held to maturity. All PCA investments were short-term and had been placed in investment grade instruments. Following is a description of these investments:

	2009		2008	
	Book Value	**Fair Value**	**Book Value**	**Fair Value**
Investment securities:				
Investments in multilaterals	-	-	27,969	28,232
Investments in commercial paper and financial bonds	-	-	235,450	229,547
Investments in commercial paper and non-financial bonds	-	-	207,007	205,947
	-	-	470,426	463,726

Changes in investments held to maturity are stated as follows:

	2009	2008
Balance at the beginning of the year	470,426	335,162
Additions	-	649,170
Redemptions	(470,426)	(513,906)
Balance at the end of the year	-	470,426

7. Hedge instrument

In fiscal year 2009, the hedge instrument consisted of a time deposit in Euros whose objective was to hedge the exposure to variability in foreign exchange rates as a result of the obligation to pay for the fabrication and acquisition of a dredge in this currency. The delivery of the dredge is planned for fiscal year 2011.

(In thousands of balboas)

The fair value of the financial instrument was measured using the Bloomberg exchange rate in EUR-USD at the closing of September 30, 2009.

The hedge instrument activity is detailed as follows:

	2009	**2008**
Hedge instrument - time deposit	50,979	-
Hedge instrument valuation adjustment	6,478	-
	57,457	-

8. Accounts receivable

Accounts receivable are detailed as follows:

	2009	**2008**
Transit-related services	10,056	6,427
Electric power sales	16,989	23,934
National Institute of Pipelines and Sewerage (Instituto de Acueductos y Alcantarillados Nacionales)	3,461	2,190
Other government entities	1,370	1,140
Other services	1,738	1,501
	33,614	35,192

9. Inventories, net

The inventories are detailed as follows:

	2009	**2008**
Supplies and materials	44,438	37,428
Fuel	11,920	8,938
Provision for obsolete inventory	(6,705)	(6,505)
	49,653	39,861

(In thousands of balboas)

Change in the provision for obsolete inventory of supplies and materials is as follows:

	2009	**2008**
Balance at the beginning of the year	6,505	6,400
Increase	590	772
Charges	(390)	(667)
Balance at the end of the year	6,705	6,505

10. Retained earnings reserved

Article 41 of the Organic Law establishes that after covering the costs for operation, investment, modernization, and expansion of the Canal, as well as the necessary reserves provided by the Law and the Regulations, any surplus shall be forwarded to the National Treasury in the following fiscal period.

Changes in reserved retained earnings are detailed as follows:

	September 30, 2009			
	Balance at the beginning of the year	**Increase**	**Decrease**	**Balance at the end of the year**
Reserves for:				
Canal expansion	91,306	-	-	91,306
Investment projects - others	25,000	40,000	-	65,000
Catastrophic risks	36,000	-	-	36,000
Social and environmental program of the Canal watershed	10,000	-	-	10,000
Contingencies and working capital	157,679	889	-	158,568
Enterprise capitalization	243,871	24,036	-	267,907
	563,856	64,925	-	628,781
Contributions for:				
Investment programs	1,595,905	507,868	-	2,103,773
	2,159,761	572,793	-	2,732,554

(In thousands of balboas)

	September 30, 2008			
	Balance at the beginning of the year	**Increase**	**Decrease**	**Balance at the end of the year**
Reserves for:				
Canal expansion	35,300	56,006	-	91,306
Investment projects - others	-	25,000	-	25,000
Catastrophic risks	36,000	-	-	36,000
Social and environmental program of the Canal watershed	10,000	-	-	10,000
Contingencies and working capital	142,978	14,701	-	157,679
Enterprise capitalization	234,000	9,871	-	243,871
	458,278	105,578	-	563,856
Contributions for:				
Investment programs	1,016,873	579,032	-	1,595,905
	1,475,151	684,610	-	2,159,761

The equity reserves established up to date are as follows:

Reserve for Canal expansion
The Board of Directors approved an equity reserve for the construction program of the Panama Canal third set of locks. The funds for this reserve are segregated based on the levels of earnings obtained, according to the financing needs of the PCA for determined projects during the implementation of the program. The Board of Directors approved a reserve of B/.56,006 for fiscal year 2008, whereas in fiscal year 2009, the PCA did not increase this reserve.

Reserve for investment projects - others
The Board of Directors approved an equity reserve for the investment programs in the Panama Canal. The funds of this reserve are segregated based on the earning levels, according to PCA's financing needs for particular projects during programs execution. During fiscal year 2009, the Board of Directors approved a reserve of B/.40,000 for a total reserve of B/.65,000 (2008: B/.25,000).

Reserve for catastrophic risks
The Board of Directors approved an equity reserve to cover the deductibles of the catastrophic risks insurance policies with a maximum amount of B/.36,000. The PCA did not increase this reserve for fiscal years 2009 and 2008.

Reserve for the social and environmental program of the Canal watershed
The Board of Directors approved the establishment of a reserve to finance the social and environmental program of the Canal watershed. The purpose of this program is to preserve natural resources and promote the development and integral management of the watershed. During fiscal years 2009 and 2008, the PCA did not make appropriations to this reserve.

Reserve for contingencies and working capital
The Board of Directors approved an equity reserve for contingencies and working capital based on the PCA's level of revenues. The amount of this reserve is based on the average of 30 days of Canal revenues or billing, and is funded in stages, periodically, as agreed by the Board of Directors. During fiscal year 2009, the Board of Directors approved the increase of this reserve by B/.889 (2008: B/.14,701) for a total reserve of B/.158,568 (2008: B/.157,679).

Enterprise capitalization
The Board of Directors approved a reserve for Enterprise capitalization. The purpose of this reserve is to ensure and facilitate the long-term financial projection of the Enterprise. This reserve will be funded in stages, according to the periodicity agreed by the Board of Directors. During fiscal year 2009, the Board of Directors approved the increase of this reserve by B/.24,036 (2008: B/.9,871) for a total of B/.267,907 (2008: B/.243,871).

Contributions to investment programs
The Board of Directors approved an increase in funds to investment programs for B/. 507,868 (2008: B/.579,032).

(In thousands of balboas)

11. Unappropriated retained earnings

Article 41 of the Organic Law establishes that after covering the costs for the investment program and the reserves detailed in Note 10, any surplus shall be remitted to the Panamanian Treasury in the following fiscal period. Therefore, the PCA should transfer the total amount of B/.434,120 to the Panamanian Treasury which corresponds to the year ended September 30, 2009 (2008: B/.343,852).

In compliance with Law 28 of 2006, during the construction period of the third set of locks, the PCA will continue to make increasing payments to the Panamanian Treasury based on Canal tonnage fees and any operational surplus. Any payments based on an operational surplus shall not be less than those made to the Panamanian Treasury in 2005 for the amount of B/.268,850. The combined payments based on Canal tonnage fees and operational surpluses shall not be less than the payments effected in fiscal year 2006 for the amount of B/.568,128.

12. Accounts payable

The accounts payable are as follows:

	2009	2008
Panamanian Treasury	26,753	27,460
Suppliers and others	99,150	91,898
	125,903	119,358

Article 39 of the Organic Law establishes that the PCA shall pay annually the Panamanian Treasury a fee per net ton, or its equivalent, collected from vessels paying tolls for use of the Canal. This fee shall be set by the PCA. The total of such fees amounted to B/.344,320 (2008: B/.355,034) for the year ended September 30, 2009.

The balance payable to the Panamanian Treasury is mainly represented by the fee per net ton payment that is outstanding at September 30, 2009.

(In thousands of balboas)

13. Provision for marine accident claims

The provision for marine accident claims of B/.32,368 (2008: B/.27,474), represents the estimated value of filed or anticipated claims for accidents in Canal waters for which the PCA expects to be liable.

The PCA carries out investigations to determine the cause of each marine accident. When the cause of the accident is determined, the PCA records, if applicable, a provision based on an estimate of the vessel's permanent and temporary repair costs that in the opinion of management, is the PCA's responsibility. The amount of the provision is reviewed at the balance sheet date, and if necessary, it is adjusted to reflect the best estimate at that moment.

Changes in the provision for marine accident claims are detailed, as follows:

	2009	**2008**
Balance at beginning of the year	27,474	29,883
Provision for the year	7,410	642
Payments made	(2,516)	(3,051)
Balance at end of the year	32,368	27,474

The increase in the provision is included as an expense of the current period under "Provision for Marine Accidents."

14. Capitalized labor and materials

During the execution of the Investment Program - others and Investment Program - Canal expansion, the PCA utilizes the services of contractors as well as its own resources and equipment.

In both Investment Programs, the internal cost transfers of labor, materials and supplies, use of equipment (fuel, maintenance and depreciation), and other expenses attributable to the investments made with the PCA's own resources and equipment are originally recorded as operating expenses as incurred. These costs are later credited in the income statement of the period in which they were incurred and charged to the construction in progress account of properties, plant and equipment.

(In thousands of balboas)

The direct costs incurred for personal services in the Investment Program - Canal expansion, and the contracted services in the investment projects of both programs, are charged directly to the construction in progress account of property, plant and equipment.

The most significant projects of the investment program that have been executed with PCA's own resources and equipment are detailed as follows:

	2009	**2008**
Investment Program - Others:		
Widening and straightening of the Gaillard (Culebra) Cut	8,870	9,147
Deepening of Gatun Lake and Gaillard (Culebra) Cut	-	6,768
Rehabilitation of tow tracks	-	2,025
Rehabilitation of barges 403 y 407	389	1,500
Replacement of turntables in Gatun Locks	-	798
New tie-up Station for vessels in Cartagena Hill	-	672
Procurement and installation of hydraulic operators for the rising stem valves	-	645
Purchase of tow components	3,457	-
Project administration system	706	-
Replacement of the vehicular gates with a vehicular bridge	466	-
Other various projects	1,841	2,576
	15,729	24,131

(In thousands of balboas)

	2009	2008
Investment Program - Canal Expansion:		
Dredging of Gatun Lake	39,135	24,370
Deepening of Gaillard (Culebra) Cut	-	4,500
Dredging at the Pacific entrance	3,417	-
Dry excavation No. 4 of the North Pacific channel access and construction of Borinquen's dam	713	803
Program administration	628	-
Construction of new field offices for the new Locks	440	-
Excavation project No. 2	392	-
Disposal site studies in the Atlantic Side	321	-
Studies and specifications in all Locks	-	299
Other various projects	860	1,608
	45,906	31,580
Total capitalized	61,635	55,711

15. Income taxes

The PCA is not subject to income taxes, as stated in Article 43 of the Organic Law which exempts it from the payment of all national or municipal taxes, except for the employer's contribution of social security, educational insurance, workmen's compensation, fees for public services, and the fee per net ton.

16. Contributed capital

Article 316 of the Political Constitution of the Republic of Panama states that, PCA has its own patrimony and the right to manage it.

Upon the transfer of the Canal to the Republic of Panama at noon on December 31, 1999, PCA became the administrator of all personal and real estate property identified in the Organic Law of PCA as the patrimony necessary to operate and maintain the Canal.

This patrimony is divided into two groups: the inalienable patrimony, comprised of land, lakes, rivers, dams, locks and anchorages, as established in Article 2 of the Organic Law; and the economic patrimony, comprised of all those installations, buildings, structures and equipment that support the operation of the Canal, as established in Article 33 of the same Law.

In compliance with these requirements, the Government of Panama transferred the related land and buildings to PCA. In order to record the assets transferred by the Government of Panama as part of PCA's patrimony, a conservative method was used to reflect an estimated fair value for each asset subsequently registered in the Public Registry.

17. Other miscellaneous revenues

In May 1999, the Panama Canal Commission, prior to its dissolution and liquidation, transferred B/.10,000 to PCA to establish a severance fund for compensation payments that would cover the time of service of former Panama Canal Commission (PCC) employees hired by the PCA who could be involuntarily terminated from their positions after being contracted. During fiscal year 2008, the Board of Directors authorized the Administration to reverse this provision as there had been no involuntary employee terminations which have required the disbursement. This provision of B/.10,000 was reversed and recorded as "other miscellaneous revenues" in fiscal year 2008.

18. Remunerations and benefits to key managers

The PCA paid remunerations and benefits to key managers for a total of B/. 2,183 (2008: B/.1,487). During fiscal year 2009, various managers received payment of a portion of their benefits corresponding to fiscal year 2008. Additionally, during fiscal year 2009, various managers were promoted to key positions.

19. Risk Management of Financial Instruments

Investment securities
During fiscal year 2008, investment consisted of bonds which had been acquired with the intention of being held to maturity. All PCA investments were short-term and have been placed in investment grade instruments.

Hedge instrument
In fiscal year 2009, the cash flow hedge instrument consisted of a time deposit in Euros. The objective of this instrument was to hedge the exposure to volatility in Euro rates as a result of the obligation of payment in this currency for the fabrication and acquisition of a dredge.

Risk management of investments in securities and hedge instrument
Article 44 of the Financial Management Regulation, in accordance with Article 190 of the Regulation on PCA Purchasing and Contracts, establishes that PCA could hedge contracts with specialized institutions in an effort to mitigate the risks associated with fluctuations of:

- Prices of commodities acquired by the PCA or its contractors for the purpose of the functioning, maintenance, operation, modernization and the expansion of the Canal.
- Interests rates on loans or other credit obligations assumed by the PCA.
- The exchange rates of foreign currencies in relation to the ones of legal tender in the Republic of Panama when the PCA has incurred obligations in foreign currencies.

The specialized institutions which provide these services must have a risk qualification in conformity with the established Policies Applicable to the Contracting of Risk Mitigation Services through Hedge Financial Instruments.

The Board of Directors established through Agreement No. 170 of October 30, 2008, that all investments of the PCA, deposits and/or certificates of deposits, be made in currencies of the United States of America or in other currencies, exclusively for the payment to vendors for contracts awarded under conditions and payments with such currencies, without the intention of speculating and only to mitigate the currency exchange risk.

With the purpose of minimizing financial risks, the Board of Directors, through Agreement No. 179 of January 28, 2009, determined not to invest in other financial instruments different from time deposits, until December 31, 2009.

On May 19, 2009, through Agreement No. 185, the Board of Directors established that investments in financial instruments could not be done, without a corresponding approved investment policy for such instruments.

On September 24, 2009, through Agreement No. 195, the Board of Directors established criteria and guidelines for the investment of liquid assets, which authorize the investment in financial instruments through the application of the Banking Institutions and Financial Instruments Risk System.

The PCA's Finance Committee of the Board of Directors is responsible for presenting a conservative investment policy to the Board of Directors for its consideration with the purpose of preserving the capital and generating a reasonable return at low risk levels.

The PCA's Liquidity Investment Committee is responsible for executing the investment policy as approved by the Board of Directors.

The main risks that have been identified by the PCA include credit risks, counterparty risks, market risks, and liquidity risks.

19.1 Credit Risk

The risk that the debtor or issuer of a financial asset may fail to make any payments, completely and on time, pursuant to the terms and conditions agreed at the time of acquisition. To mitigate credit risk, the investment policy establishes limits per industry and per issuer per the results of the categorization of the Risk Assessment System adopted by the PCA. The Risk Assessment System includes the following factors: short-term risk rating, financial leverage ratios, economic factor, liquidity index, and deterioration index.

19.2 Counterparty Risk

The risk that counterparty may fail to liquidate the transactions involved in the purchase of securities. The PCA has no counterparty risks as all of its securities are purchased by means of the delivery versus payment method through a compensation system in a custody account.

19.3 Market Risk

The risk that the value of a financial asset will drop due to changes in interest rates, in foreign currency exchange rates, or due to the impact of other financial variables which are beyond the control of the PCA.

The PCA's investment policy establishes that all PCA investments and deposits shall be made in the legal tender of the United States of America, except in the event that the obligation exists to pay vendors in foreign currency.

19.3.1 Exchange Rate Risk Management Policy

The PCA has established a policy to manage its foreign exchange rate risk in relation to its currency for operations. The PCA is required to hedge all or a portion of the exposure to foreign exchange rate risk through its Treasury Department. To manage their foreign exchange risk arising from future commercial transactions and recognized assets and liabilities, the Administration places deposits in the same currency the liability or commitment is denominated

The Administration's policy is to hedge all expected cash flows, mainly for equipment purchases denominated in a currency that is not the functional currency. As of September 30, 2009, the PCA had a commitment to purchase a dredge for €38.9 million. For the purpose of hedge accounting, this purchase meets the requirements to be considered an exposure associated with "highly probable" forecasted transactions. When the future purchase takes place the PCA will adjust the amount of the non financial item that was hedged.

Sensitivity to exchange rate risk

The foreign exchange rate dollar/euro at the closing of September 30, 2009, was 1.4640 (Source: Bloomberg). If the currency had weakened/strengthened against the US dollar by 0.10, with all other risk factors held constant, the unrealized gain/loss that would have to be recorded in the equity account - adjustment for valuation of the hedging instrument – would have been B/.3.9 million.

19.3.2 Commodity price risk management policy

The PCA is exposed to the risk of fluctuations of commodity prices, mainly from the fuel used in maritime operations and power generation activities and for the sale of surplus energy to Panama's National Grid, to the extent that such variations cannot be transferred to PCA customers.

The PCA uses approximately 10 million gallons of diesel annually for ship transit operations. As of October 20, 2009, the risk of diesel price fluctuations is managed mainly during the fiscal year, as this period is considered to be representative of the implementation of appropriate commercial policies. This process is carried out by means of specific hedging activities for 80% of the forecasted volume, with the objective of maintaining an economic balance of commodities.

The PCA's power generation activity is used for internal consumption as well as for third-party commercialization. The PCA consumes approximately 20% of the energy produced while the remaining 80% is sold to third parties. The energy is produced by hydroelectric plants (28%) and by thermal plants (72%). In fiscal year 2009, internal consumption represented 18.4 % of production, while the surplus sold in Panama's energy market represented the remaining 81.6%. Thermal generation is exposed to the risk of fuel price variation. The major part of the exposure to this residual risk is managed by means of periodically renegotiated contractual clauses that have the objective of achieving economic balance for the consumption of the related fuel.

Sensitivity to fuel price risk associated with operations

As of September 30, 2009, the prevailing diesel price index for purchases of the PCA was B/.1.74 per gallon. With an estimated annual consumption of 10 million gallons, assuming a variation that increases the diesel price to B/.2.30 per gallon during fiscal year 2010, the fuel expense would increase or decrease of approximately B/.3.5 million, as long as the price remains under the price agreed upon in the hedging instrument.

19.3.3 Escalation clauses in contracts related to the Canal Expansion and Modernization Program

As mentioned in Note 20, the PCA has different commitments related to the Canal Expansion and Modernization Program. These commitments include escalation clauses related to the main commodities that will be used during construction such as: reinforced steel, cement, structural steel, and light diesel. The clauses use as adjustment reference factors, price indexes of the commodities' fair value, a fixed reference price for each material, the quantities or maximum volume, and target dates for escalation performance.

(In thousands of balboas)

The maximum volume amounts to which the PCA is exposed during the execution of this project are the following:

Raw material	**Agreed volume (thousands)**	**Reference fixed price**	**Fair value reference index**
Reinforced steel	279.0 metric tons	$575 per metric ton	*Reinforcing Bar - Platts Steel Market Daily"*
Structural steel	67.2 metric tons	$1,000 per metric ton	*"Plate - Platts Steel Market Daily"*
Cement	1,278.6 short tons	$100 per short ton	*"Portland and Other Cements, Commodity Code 13220161"* del US Bureau of Labor Statistics.
Light diesel (Third Set of Locks contract)	60,000 gallons	$1.40 per gallon	*US Gulf Coast Diesel No.2 Oil* de *Platts Latin American Wire*
Light diesel (Pacific Access Channel excavation contracts)	2,054 gallons	$1.7580 per gallon	*Import Parity Price for light diesel as described by Panamanian Energy Secretary*

For the life of the project, the PCA shall determine the fair value of the commodities to be used during the periods established in its proposal, for the purpose of then determining the difference with the referenced fixed price. This price difference shall be multiplied by the agreed volumes to obtain the amount over that which the PCA must pay or charge the contractor during periodic payments for work progress. In addition, the contract for the construction of the locks allows for the covering of a portion of the incremental cost associated exclusively with local labor, as it was conceived to cover solely the cost overrun of Panamanian labor.

(In thousands of balboas)

Sensitivity to the risk associated with escalation clauses in the contracts related to the Canal Expansion and Modernization Program

To analyze the effect of a possible variation in the price of light diesel on the cost of the Canal expansion and modernization program, an analysis was performed assuming an upward variation that takes the price of diesel to a value of B/.2.30 per gallon during fiscal year 2010. For an estimated total consumption of 4.7 million gallons during that period, and while keeping all other variables constant, this variation impacts the fuel expense item in approximately B/.3.1 million.

For fiscal year 2010, no consumption of cement, reinforced steel, or structural steel has been forecasted.

19.4 Liquidity management policy

The risk that an entity will have difficulties in meeting commitments associated with financial liabilities.

The PCA's Treasury monitors on a daily basis the available liquidity levels after fulfilling the PCA's funding needs and to avoid overdrafts.

In regards to liquidity management, the Authority is exposed to the effects of market interest rate fluctuations on its short-term investments, which result in variations in interest earnings. To partially mitigate this risk, the liquidity is placed for terms of up to 12 months, depending on expectations about interest rates.

Liquidity investment as of September 30, 2009

(millions of balboas)	Up to 30 days	31 to 90 days	91 to 180 days	181 to 270 days	271 to 365 days	Total
Investment securities	-	-	-	-	-	-
Time deposits	-	65	1,274	794	227	2,360

(In thousands of balboas)

Sensitivity to interest rate risk

To calculate the effect of a possible variation of reference interest rates (Libor) on time deposits, an analysis was performed as of September 30, 2009, assuming variations of 25 basis points lower/higher. With all other variables held constant, this variation would impact the Authority's net income due to the increase or decrease in revenues from interests earnings in the amount of B/. 4.9 million.

20. Contingent liabilities and commitments

Contingent liabilities

PCA has received claims and is a defendant in various legal proceedings mainly related to marine accidents. The PCA's contingent liabilities amounted to approximately B/.1,763 (2008: B/.1,903) corresponding to marine accident claims. The opinion of management and its legal advisors is that the outcome of these matters is not likely to have a material adverse effect on the PCA's financial position.

Commitments

Commitments as a result of incomplete construction contracts and undelivered purchase orders amounted to approximately B/.3,757,000 (2008: B/.554,000), as follows:

	2009	**2008**
Investment programs:		
Canal Expansion	3,435,000	230,000
Others	259,000	276,000
Operations	63,000	48,000
	3,757,000	554,000

Total commitments include the Canal expansion program contracts awarded during the fiscal year totaling B/.3,360,426 (2008:B/.229,280). The total costs incurred in the Canal expansion program in the fiscal year amounted to B/.249,583 (2008:B/.102,435).

On July 15, 2009, the PCA awarded the design-build contract for the Canal Expansion Program's major component, the third set of locks, to Grupo Unidos por el Canal (GUPC), for B/.3,221,631. GUPC is composed by the corporations Sacyr Vallehermoso S.A. (Leader) (Spain), Impregilo S.P.A. (Italy), Jan de Nul n.v (Belgium) and Constructora Urbana, S.A. (Panama).

On August 11, 2009, the consortium submitted the B/.400,000 performance bond as well as the B/.50,000 payment bond as required by the PCA, and the PCA subsequently issued the order to proceed by which GUPC is requested to initiate all related work by August 25, 2009 and deliver the project within a period of 1,883 days.

The PCA will make a B/.300,000 advance and mobilization payment to GUPC during the first quarter of 2010, once the contractor has complied with all the requirements established in the contract terms and conditions.

Canal Expansion Finance Contracts
Article 319 of the Political Constitution of the Republic of Panama and the Organic Law, whereby the Panama Canal Authority is organized, establish that the Board of Directors is entitled to authorize, upon duly reasoned and supported proposal by the Administrator, the acquisition of loans and other credit obligations to make investments upon approval by the President's Cabinet and within the terms provided by this Law and the Political Constitution of the Republic.

On October 10, 2008, the Board of Directors agreed to request the approval of the President's Cabinet for the contract of loans and other credit obligations to cover the financial needs of the Expansion Program in the amount of B/.2,300,000. Consequently, the President's Cabinet, by means of Cabinet Decree No. 178 of October 13, 2008, approved the request and, in turn, on October 14, 2008, the Board of Directors authorized the Administration to proceed with the loan contracts in accordance with the terms and with the following multilateral and bilateral agencies:

Terms:

- Financing will be provided without guarantees or recourse to the Panamanian Government.
- Financing will not be subject to the binding commitment of obtaining goods or services from any particular source.
- Lenders shall not intervene in the operation or management of the Canal.
- Financing will not have an effect on payments to the National Treasury, pursuant to Law No. 28 of 2006.
- Loans maturity will not be less than twenty years, with a ten year grace period.
- Interest rate and commitments and underwriting fees will be accorded based on market conditions and at the moment of their disbursements.

The following multilateral and bilateral agencies are committed to granting loans to the PCA, as detailed below:

- The European Investment Bank (EIB), for B/.500,000.
- The Japan Bank for International Cooperation (JBIC), for B/.800,000.
- The Inter-American Development Bank (IDB), for B/.400,000.
- The International Finance Corporation (IFC), for B/.300,000.
- The Andean Development Corporation (ADC), for B/.300,000.

These resources will be available until December 9, 2014. At the date of this report, these loans have not been disbursed.

21. Fair value of financial instruments

The following assumptions were used by Management to estimate the fair value of each financial instrument category in the balance sheet:

a. *Cash, cash equivalents, and bank deposits* - The book value approximates its fair value due to its liquidity and short-term maturity.

b. *Accounts receivable* - Accounts receivable are recorded at their face value, which approximates its fair value due to its short-term maturity.

c. *Investment in securities* - Its book value is adjusted to its fair value based on market values obtained from public sources.

d. *Inventories* - These are recorded at acquisition cost, adjusted by an allowance for slow-moving or obsolete materials and supplies, and do not include profit margin.

e. *Accounts payable* - The book value of accounts payable corresponds to the cost of the transaction performed, which approximates its fair value due to its short-term maturity.

These estimates are subjective in nature, involve uncertainties and critical judgment elements, and therefore, cannot be precisely established. Any change in assumptions or criteria can significantly affect the estimates.

22. Subsequent Events

Contracts for Hedging Services

The PCA's Board of Directors approved the management process to use hedging strategies aimed at mitigating the risks related to price volatility of commodities used in the operation, maintenance, and expansion of the Canal, as well as those of capital investments, interest rates, and foreign exchange rates other than the ones of legal tender in Panama.

On September 30, 2009, the Board of Directors authorized the Administration to proceed with the contracting of hedging services for the purchase of light diesel for operations up to 9.0 million gallons, for a term of up to a year and with a maximum unit price (CAP) of B/.2.30, with the purpose of mitigating potential fluctuations in the price of this commodity. On October 20, 2009, the PCA contracted a volume of 8,522,727 gallons, which corresponds to the total purchase foreseen for fiscal year 2010.

At present, the PCA is considering the possibility of contracting hedging services to transfer to a third party the risk assumed with these escalation clauses, in order to stabilize the needs, the cost of financing, and mitigate the risk of contract over-run of the main contract. The derived instruments implicit in the contract for the design and construction of the PCA Third Set of Locks need not be separated from the main contract, since they are clearly and closely related to the economic characteristics and the risks of the main contract due to the fact that the implicit derivative has a reasonable value commonly associated to the reasonable value of the main contract. Also, the price clauses related to the indexes do not have any level of leverage and the notional volume is clearly defined and specified in the main contract.

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