



## NOTICE OF REGULAR ANNUAL STOCKHOLDERS' MEETING

NOTICE IS HEREBY GIVEN that the Regular Annual Meeting of Stockholders of **AYALA CORPORATION** will be held at the Grand Ballroom of the InterContinental Manila, Ayala Ave., Makati City, on **Friday, 04 April 2008** at **9:00 a.m.** with the following

### A G E N D A

1. Determination of Quorum
2. Approval of Minutes of Previous Meeting
3. Annual Report
4. New Business
  - 4.1 Ratification of all Acts and Resolutions of the Board of Directors and Management adopted during the preceding year in the ordinary course of business.
  - 4.2 Ratification of the Resolutions of the Board of Directors adopted on 31 January 2008:
    - 4.2.1 declaration of a 20% Stock Dividend to all holders of common shares of the Corporation as of a record date to be fixed during its Annual Stockholders' Meeting.
    - 4.2.2 re-issuance and reclassification of the redeemed 1.2 Billion Preferred "A" and "AA" Shares with a par value of ₱1.00 per share into 12 Million new Preferred "A" Shares with a par value of ₱100.00 per share, and the amendment of Article Seventh of the Amended Articles of Incorporation to reflect the same.
5. Election of Directors (including the Independent Director)
6. Election of Auditors and Fixing of their Remuneration
7. Consideration of such other business as may properly come before the meeting
8. Adjournment

Only stockholders of record at the close of business on **25 February 2008** are entitled to notice of, and to vote at, this meeting. As per By-Laws, the Stock and Transfer Books of the Corporation will be closed from **25 February to 03 March 2008**, inclusive.

Makati City, 11 February 2008.

FOR THE BOARD OF DIRECTORS

**MERCEDITA S. NOLLEDO**  
Corporate Secretary

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We are not soliciting your proxy. However, if you would be unable to attend the meeting but would like to be represented thereat, you may accomplish the enclosed proxy form and submit the same to the Office of the Corporate Secretary on or before **26 March 2008**. You may use the enclosed reply envelope for this purpose or you may send in advance the proxy form at fax no. (632) 759-4383. Validation of proxies shall be held on **28 March 2008** at 9:00 a.m. at the Office of the Corporate Secretary.

Thank you.

SECURITIES AND EXCHANGE COMMISSION

SEC FORM 20-IS

Information Statement  
of  
**AYALA CORPORATION**  
Pursuant to Section 20 of the Securities Regulation Code

1. Check the appropriate box:

Preliminary Information Sheet  
 Definitive Information Sheet

2. Name of Registrant as specified in its charter: AYALA CORPORATION
3. Province, country or other jurisdiction of incorporation or organization: REPUBLIC OF THE PHILIPPINES
4. SEC Identification Number: 34218 (PSE Security Code: HO-070)
5. BIR Tax Identification Code: 000-153-610-000
6. Address of Principal Office: 34<sup>th</sup> Floor, Tower One and Exchange Plaza  
Ayala Triangle, Ayala Avenue  
Makati City  
1226
7. Registrant's telephone number, including area code: (632) 848-5772 / 841-5453
8. Date, time and place of the meeting of security holders:

Date - 04 April 2008  
Time - 9:00 A.M.  
Place - Grand Ballroom  
InterContinental Manila  
Ayala Center, Makati City

9. Approximate date on which the Information Statement is first to be sent or given to security holders:

10 March 2008

10. Securities registered pursuant to Sections 8 and 12 of the Code or Sections 4 and 8 of the RSA:

a. Authorized Capital Stock P 37,000,000,000.00

<u>Title of Each Class</u>	<u>Par Value</u>	<u>No. of Shares</u>	<u>Authorized Capital Stock</u>
Common	P50.00	600,000,000	P30,000,000,000.00
Preferred "A"	1.00	900,000,000	900,000,000.00
Preferred "AA"	1.00	300,000,000	300,000,000.00
Preferred "B"	100.00	58,000,000	<u>5,800,000,000.00</u>
Total			<u>P37,000,000,000.00</u>

**b. Number of Shares Outstanding as of 31 December 2007**

<u>Title of Each Class</u>	<u>Par Value</u>	<u>No. of Shares</u>	<u>Authorized Capital Stock</u>
Common	₱50.00	414,363,423*	₱20,718,171,150.00
Preferred "B"	100.00	58,000,000	<u>5,800,000,000.00</u>
Total			<u>₱26,518,171,150.00</u>

\* Net of 323,622 Treasury Shares

**c. Amount of Debt Outstanding as of 31 December 2007**

Current and Long Term Debt ₱ 50.0 billion

**11. Are any or all of registrant's securities listed in a Stock Exchange?**

Yes  No

A total of 412,298,086 Common shares and 58,000,000 Preferred "B" shares are listed with the Philippine Stock Exchange as of 31 December 2007, excluding: i) the 2,226,328 Common shares allotted for the stock option/ownership plans of the Company, the listing of which was approved in principle by the PSE; ii) the re-issuance of Treasury Shares of 153,718 Common shares; iii) the 333 Common shares representing the underlying shares for the conversion of Preferred Shares; iv) the issuance of 958 Common shares to the minority holders of PF Prime Properties, Inc. pursuant to its merger into the Company and which was approved and licensed by the SEC; and v) the 316,000 Common shares bought under the Share Buyback Program of the Company which were previously listed with the PSE.

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## INFORMATION REQUIRED IN INFORMATION STATEMENT

### A. GENERAL INFORMATION

#### Item 1. Date, time and place of meeting of security holders

- a. Date - 04 April 2008  
Time - 9:00 A.M.  
Place - Grand Ballroom  
InterContinental Manila  
Ayala Center, Makati City
- Principal Office - 34<sup>th</sup> Floor, Tower One and Exchange Plaza  
Ayala Triangle, Ayala Avenue  
Makati City  
1226
- b. Approximate date when the Information Statement is first to be sent to security holders: 10 March 2008

**WE ARE NOT ASKING YOU FOR A PROXY AND YOU  
ARE REQUESTED NOT TO SEND US A PROXY**

#### Item 2. Dissenter's Right of Appraisal

The ratification of the Resolution of the Board of Directors recommending the re-issuance and reclassification of the redeemed 1.2 Billion Preferred "A" and "AA" Shares with a par value of ₱1.00 per share into 12 Million new Preferred "A" Shares with a par value of ₱100.00 per share, and the amendment of Article Seventh of the Amended Articles of Incorporation to reflect the same, may give rise to a possible exercise by security holders of their appraisal right under Title X of the Corporation Code of the Philippines.

A stockholder who shall have voted against the aforesaid proposed action (the "dissenting stockholder") may exercise his appraisal right by making a written demand on the Company within 30 days after the Stockholders' Meeting date. Failure to make the demand within the prescribed period shall be deemed a waiver of the appraisal right. If the proposed corporate action is implemented, the Company shall pay the dissenting stockholder upon surrender of the stock certificates representing his shareholdings in the Company based on the fair value thereof as of the day prior to the date of the Stockholders' Meeting, excluding any appreciation or depreciation in anticipation of such corporate action, provided that no payment shall be made to the dissenting stockholder unless the Company has unrestricted retained earnings to cause such payment.

#### Item 3. Interest of Certain Persons in or Opposition to Matters to be Acted Upon

There is no matter to be acted upon in which any Director or Executive Officer is involved or had a direct, indirect or substantial interest.

No Director has informed the Company of his opposition to any matter to be acted upon.

### B. CONTROL AND COMPENSATION INFORMATION

#### Item 4. Voting Securities and Principal Holders Thereof

- a. Number of Shares Outstanding as of 31 January 2008: 413,869,423 Common shares  
(net of 817,622 Treasury Shares)
- 58,000,000 Preferred "B" shares

Number of Votes Entitled:

one (1) vote per share for Common shares

One (1) vote per share for Preferred shares on matters provided for under the Corporation Code

- b. All stockholders of record as of 25 February 2008 are entitled to notice and to vote at the Annual Stockholders' Meeting

**c. Manner of Voting**

Article III Sections 7 and Section 8 of the Amended By-Laws of the Company provide:

“Section 7.- Each share of stock entitles the person in whose name it is registered in the books of the Corporation to one vote, provided the conditions as regards payment subject to which it was issued have been complied with.”

“Section 8 - The election of Directors shall be by ballot and each stockholder entitled to vote may cast the vote to which the number of shares he owns entitles him, for as many persons as are to be elected as Directors, or he may give to one candidate as many votes as, the number of Directors to be elected multiplied by the number of his shares shall equal, or he may distribute them on the same principle among as many candidates he may see fit, provided that the whole number of votes cast by him shall not exceed the number of shares owned by him multiplied by the whole number of Directors to be elected. x x x ”

**d. Security Ownership of Certain Record and Beneficial Owners and Management**

- i. Security Ownership of Certain Record and Beneficial Owners (of more than 5%) as of 31 January 2008.

<b>Title of Class</b>	<b>Name, address of Record Owner and Relationship with Issuer</b>	<b>Name of Beneficial Owner and Relationship with Record Owner</b>	<b>Citizenship</b>	<b>No. of Shares Held</b>	<b>Percent (of the Outstanding Common Shares)</b>
Common	Mermac, Inc. <sup>1</sup> 35/F Tower One, Ayala Triangle, Ayala Ave., Makati City	Mermac, Inc. <sup>2</sup>	Filipino	210,895,275	50.96%
Common	PCD Nominee Corporation (Non-Filipino) <sup>3</sup> G/F MSE Bldg. Ayala Ave., Makati City	Hongkong and Shanghai Banking Corporation (HSBC) and Standard Chartered Bank (SCB) <sup>4</sup>	Various	111,677,732	26.98%
Common	Mitsubishi Corporation <sup>5</sup> 14/F L.V. Locsin Bldg. 6752 Ayala Ave., Makati City	Mitsubishi Corporation <sup>6</sup>	Japanese	43,803,848	10.58%

<sup>1</sup> The Co-Vice Chairmen of Mermac, Inc. (“Mermac”), Jaime Augusto Zobel de Ayala and Fernando Zobel de Ayala, are the Chairman/CEO and President/COO of the Company, respectively.

<sup>2</sup> The Board of Directors of Mermac has the power to decide how Mermac shares in Ayala are to be voted.

<sup>3</sup> The PCD is not related to the Company.

<sup>4</sup> HSBC and SCB are participants of PCD. The 63,831,501 and 27,048,341 shares beneficially owned by HSBC and SCB, respectively, form part of the 132,747,482 shares registered in the name of PCD Non-Filipino and Filipino. The clients of HSBC and SCB have the power to decide how their shares are to be voted. There no holders of more than 5% of the Company’s shares under HSBC and SCB.

<sup>5</sup> Mitsubishi Corporation (“Mitsubishi”) is not related to the Company.

<sup>6</sup> The Board of Directors of Mitsubishi has the power to decide how Mitsubishi shares in Ayala are to be voted.

Common	PCD Nominee Corporation (Filipino) G/F MSE Bldg. Ayala Ave., Makati City	Hongkong and Shanghai Banking Corporation (HSBC) and Standard Chartered Bank (SCB)	Filipino	21,069,750	5.09%
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ii. Security Ownership of Directors and Management as of 31 January 2008.

Title of Class	Name of Beneficial Owner	Amount and Nature of Beneficial Ownership	Citizenship	Percent of All Class
<i>Directors</i>				
Common	Jaime Augusto Zobel de Ayala	261,711 (direct)	Filipino	0.055463%
Common	Fernando Zobel de Ayala	273,270 (direct)	Filipino	0.057912%
Common	Meneleo J. Carlos, Jr.	1 (direct)	Filipino	0.000000%
Common	Toshifumi Inami	1 (direct)	Japanese	0.000000%
Common	Delfin L. Lazaro	136,926 (direct)	Filipino	0.029018%
Common	Xavier P. Loinaz	87,928 (direct)	Filipino	0.018634%
Common	Mercedita S. Nollo do	114,090 (direct)	Filipino	0.024178%
<i>CEO and Most Highly Compensated Officers</i>				
Common	Jaime Augusto Zobel de Ayala	261,711 (direct)	Filipino	0.055463%
Common	Fernando Zobel de Ayala	273,270 (direct)	Filipino	0.057912%
Common	Delfin L. Lazaro	136,926 (direct)	Filipino	0.029018%
Common	Rufino Luis T. Manotok	131,752 (direct & indirect)	Filipino	0.027921%
Preferred "B"		25,000 (direct)		0.005298%
Common	Mercedita S. Nollo do	114,090 (direct)	Filipino	0.024178%
Common	Renato O. Marzan	81,074 (direct & indirect)	Filipino	0.017181%
Common	Ramon G. Opulencia	93,148 (direct & indirect)	Filipino	0.019740%
Preferred "B"		15,000 (direct)		0.003178%
Common	Alfredo I. Ayala	37,500 (direct)	Filipino	0.007947%
Common	Victoria P. Garchitorena	68,742 (direct)	Filipino	0.014568%
Common	Solomon M. Hermosura	78,240 (direct & indirect)	Filipino	0.016581%
Common	Ricardo N. Jacinto	23,859 (direct & indirect)	Filipino	0.005056%
Preferred "B"		48,982 (direct)		0.010380%
Common	Mark Anthony N. Javier	43,106 (direct)	Filipino	0.009135%
Common	Rufino F. Melo III	34,009 (direct & indirect)	Filipino	0.007207%
Common	John Philip S. Orbeta	57,008 (direct)	Filipino	0.012081%
Common	Luis Juan B. Oreta	55,051 (direct & indirect)	Filipino	0.011666%
<i>Other Executive Officers (Group ManCom Members)</i>				
Common	Gerardo C. Ablaza, Jr.	84,716 (direct & indirect)	Filipino	0.017953%
Common	Antonino T. Aquino	50,863 (direct)	Filipino	0.010779%
Common	Jaime I. Ayala	21,105 (direct & indirect)	Filipino	0.004473%
Common	Charles H. Cosgrove	0	American	N/A
Common	Arthur R. Tan	164,836 (direct & indirect)	Filipino	0.034933%
<b>All Directors and Officers as a group</b>		<b>1,987,918</b>		<b>0.421286%</b>

None of the members of the Company's directors and management owns 2.0% or more of the outstanding capital stock of the Company.

iii. **Voting Trust Holders of 5% or More**

The Company knows of no person holding more than 5% of common shares under a voting trust or similar agreement.

iv. **Changes in Control**

No change of control in the Company has occurred since the beginning of its last fiscal year.

## Item 5. Directors and Executive Officers

Article III Section 9 of the Company's By-Laws provides:

“Section 9 - At the Regular General Meetings, a Board of seven (7) Directors shall be elected who shall hold office for a term of one (1) year or until their successors shall have been elected and qualified.”

The record of attendance of the Company's directors during the board meetings and stockholders' meeting held for the year 2007 is indicated below as follows:

Director	Regular Meetings				Annual Stockholders' Meeting & Organizational Meeting	Percentage
	March 15	June 14	Sept. 20	Dec. 6	March 30	
Jaime Augusto Zobel de Ayala	P	P	P	P	P	100%
Fernando Zobel de Ayala	P	A	P	P	P	80%
Mercedita S. Nolleto	P	P	P	P	P	100%
Meneleo J. Carlos, Jr.	P	P	P	P	P	100%
Xavier P. Loinaz	P	P	P	P	P	100%
Toshifumi Inami	P	P	P	P	P	100%
Delfin L. Lazaro	A	P	P	A	P	60%

*Legend:*

P – Present

A – Absent

The Management Committee members and other Officers of the Company, unless removed by the Board of Directors, shall serve as such until their successors are elected or appointed.

### a. Information required of Directors and Executive Officers

- i. Directors and Executive Officers – Please refer to Annex “A”

The following have been nominated to the Board of Directors of the Company for the ensuing year:

JAIME AUGUSTO ZOBEL DE AYALA  
MENELEO J. CARLOS, JR.  
DELFIN L. LAZARO  
MERCEDITA S. NOLLEDO

FERNANDO ZOBEL DE AYALA  
TOSHIFUMI INAMI  
XAVIER P. LOINAZ

The aforementioned nominees were formally nominated to the Nominations Committee of Ayala Corporation (composed of Jaime Augusto Zobel de Ayala, Fernando Zobel de Ayala and Meneleo J. Carlos, Jr.) by a shareholder of the Company, Ms. Evangeline D. Decena. In addition, Mr. Meneleo J. Carlos, Jr., an incumbent director, is being nominated as an independent director. Ms. Decena is not related to any of the nominees including Mr. Carlos. Please refer to Annex “A” for the summary of the directors' qualifications.

The nominees have served as directors of the Company for more than five years except for Mr. Meneleo J. Carlos, Jr. who has served as director for five years. Messrs. Xavier P. Loinaz, Toshifumi Inami and Delfin L. Lazaro were elected to the Board in April 2006, June 2006 and January 2007, respectively. Ms. Mercedita S. Nolleto was re-elected to the Board in 2004.

The above named nominees are expected to attend the scheduled Annual Stockholders' Meeting.

The Company has adopted the SRC Rule 38 (Requirements on Nomination and Election of Independent Directors) and compliance therewith has been made. The Company always undertakes to abide by the existing SRC Rule 38 on the required number of independent directors subject to any revision that may be prescribed by the Securities and Exchange Commission.

ii. **Significant Employees**

The Company considers its entire work force as significant employees. Everyone is expected to work together as a team to achieve the Company's goals and objectives.

iii. **Family Relationships**

Jaime Augusto Zobel de Ayala and Fernando Zobel de Ayala, Chairman/Chief Executive Officer and President/Chief Operating Officer of the Company, respectively, are brothers.

iv. **Involvement in Certain Legal Proceedings**

Except as disclosed herein, there are no material pending legal proceedings for the past five years and the preceding years until 31 January 2008 to which Ayala or the Directors or Executive Officers is a party or of which any of its material properties are subject in any court or administrative agency of the Government.

*Ayala Land, Inc.*

As of end-2007, Ayala Land, Inc. (ALI) is not involved in any litigation it considers material. However, certain individuals and entities have claimed an interest in ALI's properties located in Las Piñas, Metro Manila, which are adjacent to its development in Ayala Southvale.

Prior to purchasing the aforesaid properties, ALI conducted an investigation of the titles to the properties and had no notice of any title or claim that was superior to the titles purchased by ALI. ALI traced its titles to their original certificates of title and ALI believes that it has established its superior ownership position over said parcels of land. ALI has assessed these adverse claims and believes that its titles are in general superior to the purported titles or other evidence of alleged ownership of these claimants. On this basis, beginning in October 1993, ALI filed petitions in local regional trial courts of Makati and Las Piñas for quieting of title to nullify the purported titles or claims of these adverse claimants. A number of these cases are at various stages of trial and appeal. Some of these cases have been finally decided by the Supreme Court (SC) in ALI's favor. These include decisions affirming the title of ALI to some of these properties, which have been developed and offered for sale to the public as Sonera, Ayala Southvale. The controversy involves the remaining area of approximately 129 hectares.

ALI does not intend to develop and sell the rest of the Las Piñas properties until the litigation is resolved.

ALI has made no provision in respect of such actual or threatened litigations.

In December 1999, plaintiffs Edgardo Vazquez and Vazquez Building Systems Corporation filed a patent infringement case against Avida Land, Inc. ("Avida"), a wholly-owned subsidiary of ALI. Avida has raised a number of defenses, including the following: (i) Avida is utilizing the Tex system, a British technology patented in the Philippines of which Avida is a licensee, and not the Vasquez modular housing unit patent; (b) patent claim is overbroad; and (iii) the H-shaped column and the wall panel installation system being claimed as the infringed component cannot be covered by the Vazquez patent, because these are not patentable as they do not qualify as "novelty." In a decision dated 18 December 2007, the Regional Trial Court (RTC) of Quezon City found in favor of plaintiffs requiring Avida to compensate the plaintiffs in the amount of ₱90,000,000.00 as temperate damages or reasonable royalty with interest at the rate of six percent (6%) per annum from the date of filing of the

complaint as well as moral and exemplary damages and reasonable attorneys' fees and cost of suit. Avida filed a notice of appeal to contest this decision with the Court of Appeals (CA).

As a result of the explosion which occurred on 19 October 2007 at the basement of the Makati Supermarket Building, the Philippine National Police ("PNP") has recommended to the Department of Justice ("DOJ") the prosecution of certain officers/employees of Makati Supermarket Corporation, the owner of the building, as well as some officers/employees of ALI's subsidiary, Ayala Property Management Corp. ("APMC"), among other individuals, for criminal negligence. No criminal case has been filed by the DOJ at this time. No civil case has likewise been filed by any of the victims. In the event that the DOJ decides to file a criminal case against certain officers/employees of APMC as recommended by the PNP, the accused, if convicted after final judgment, can be held not only criminally but also civilly liable. In the event the accused will not be able to pay for the civil award, APMC will be held subsidiarily liable for such sums (the amount of which cannot be estimated). ALI and APMC believe, however, that the facts surrounding the incident do not show any negligence.

Globe Telecom, Inc.

Globe is an intervenor in and Innove is a party to Civil Case No. Q-00-42221 entitled "Isla Communications Co., Inc. et al., versus National Telecommunications Commission ('NTC') et al.," before the RTC of Quezon City by virtue of which Globe and Innove, together with other cellular operators, sought and obtained a preliminary injunction against the implementation of NTC Memorandum Circular ('MC') No. 13-6-2000 from the RTC of Quezon City. NTC MC 13-6-2000 prescribed new billing requirements for cellular service providers. The NTC appealed the issuance of the injunction to the Court of Appeals. On 25 October 2001, Globe and Innove received a copy of the decision of the CA ordering the dismissal of the case before the RTC for lack of jurisdiction, but without prejudice to the wireless companies' seeking relief before the NTC, which the CA claims had jurisdiction over the matter. On 22 February 2002, Globe and Innove filed a Petition for Review with the SC to annul and reverse the decision of the CA. The SC, on 02 December 2003, overturned the CA's earlier dismissal of the petitions filed by SMART and Globe. In its 13-page decision, the SC said that the Quezon City trial court could hear and decide the case, contrary to NTC's argument. The SC has also since denied the NTC's motion for reconsideration. Hearings are now ongoing with the RTC.

Subic Telecommunications Company, Inc. (Subictel) vs. Subic Bay Metropolitan Authority (SBMA) and Innove Communications, Inc. (Civil Case No. 155-0-2006, RTC-Branch 74, Olongapo City) On 22 May 2006, Innove received a copy of the Complaint of Subic Telecom Company ("Subictel"), Inc., a subsidiary of PLDT, seeking an injunction to stop the Subic Bay Metropolitan Authority and Innove from taking any actions to implement the Certificate of Public Convenience and Necessity granted by SBMA to Innove. Subictel claimed that the grant of a CPCN allowing Innove to offer certain telecommunications services within the Subic Bay Freeport Zone would violate the Joint Venture Agreement ("JVA") between PLDT and SBMA. Innove has since filed its Opposition to the Prayer for Injunction with Motion to Dismiss, citing that SBMA is not entitled to an injunction on the basis of the grounds it has cited in the complaint, that an injunction in this case would be contrary to public policy, and that the complaint is forum-shopping since Subictel had already previously objected to the grant of the CPCN in the proceedings before the regulatory body. SBMA also filed its Opposition pointing out, among others, that Subictel is not a proper party in this case since Subictel is not a party to the JVA. The court granted Innove's Motion to Dismiss and Subictel has filed a Motion for Reconsideration. The Motion for Reconsideration was subsequently denied and Subictel has appealed to the CA on 08 September 2006. The appeal is pending.

Manila Water Co., Inc.

*Antonio Baltazar vs. Hon. Oscar Garcia, et al., OMB Case No. C-A-05-0205-E and OMB Case No. C-A-05-0208-E, Ombudsman*

Criminal complaints were filed with the Office of the Ombudsman against members of the Board of Trustees of the Metropolitan Waterworks and Sewerage System (MWSS) and the MWSS Regulatory Office and the presidents of Manila Water Co., Inc. (MWC) and Maynilad Water Services, Inc. ("Maynilad"), for a violation of Republic Act No. 3019 and for "conduct prejudicial to the best

interests of the service.” The complaint arose from the water rate increases which became effective on 01 January 2005. MWC filed the Counter-Affidavit of its President in 2005 and is awaiting the resolution of the cases. MWC believes that the Ombudsman will dismiss the complaint.

*Freedom from Debt Coalition, et al. vs. MWSS and the MWSS-RO, G.R. No.173044, Supreme Court*

In June 2006, the Freedom from Debt Coalition petitioned the SC to annul resolutions of the MWSS Board of Trustees ruling that MWC and Maynilad are not public utilities but agents and contractors of MWSS. While MWC is not impleaded as a respondent, certain contingent, adverse, financial and regulatory consequences might result from a decision granting the petition. MWC believes that it is not a public utility but an agent and contractor of the MWSS, which remains as the public utility, a position supported by Section 2.1 of the Concession Agreement, MWSS Board Resolution dated 30 July 2004, National Water Resources Board (NWRB) Resolution dated 17 June 2005, and a Memorandum from the Office of the Government Corporate Counsel dated 01 June 2005. On 10 December 2007, the SC dismissed the petition on the following grounds: (a) petitioners should have appealed the MWSS resolutions to the NWRB instead of filing a certiorari petition with the SC; (b) the petition did not name as respondents Maynilad and MWC, the two MWSS concessionaires, who are indispensable parties; (c) petitioners disregarded the hierarchy of courts principle by filing the petition directly with the SC instead of a lower court; and (d) the case involves factual issues, which the SC cannot resolve. Recently, MWC received information that the Freedom from Debt Coalition has filed a motion for reconsideration with the SC.

**b. Certain Relationships and Related Transactions**

The Ayala Group of Companies, in their regular conduct of business, have entered into transactions with associates, joint ventures and other related parties principally consisting of advances and reimbursement of expenses, purchase and sale of real estate properties, various guarantees, construction contracts, and development, management, underwriting, marketing and administrative service agreements. Sales and purchases of goods and services to and from related parties are made at normal market prices.

No other transaction was undertaken by the Company in which any Director or Executive Officer was involved or had a direct or indirect material interest.

To date, there are no complaints received by the Company regarding related-party transactions.

**c. Ownership Structure and Parent Company**

Mermac, Inc. holds or owns 50.96% of the total issued and outstanding common stock of the Company as of 31 December 2007.

**d. Resignation of Directors**

To date, no director has resigned from, or declined to stand for re-election to the Board of Directors since the date of the 2007 annual meeting of stockholders due to any disagreement with the Company relative to the Company’s operations, policies and practices.

**Item 6. Compensation of Directors and Executive Officers**

**a. Executive Compensation**

Name and Principal Position	Year	Salary	Other Income
Jaime Augusto Zobel de Ayala Chairman and CEO			
Fernando Zobel de Ayala President and COO			
Delfin L. Lazaro			
Aristón Estrada, Jr. * Senior Managing Director			

Rufino Luis T. Manotok Senior Managing Director, Corporate Information Officer & Chief Finance Officer			
Mercedita S. Nollobo Senior Managing Director, Senior Counsel & Corporate Secretary			
Renato O. Marzan Managing Director, General Counsel, Assistant Corporate Secretary & Compliance Officer			
Ramon G. Opulencia Managing Director & Treasurer			
Alfredo I. Ayala Managing Director			
Victoria P. Garchitorena Managing Director			
Solomon M. Hermosura Managing Director			
Ricardo N. Jacinto Managing Director			
Mark Anthony N. Javier ** Managing Director			
Rufino F. Melo III Managing Director			
John Philip S. Orbeta Managing Director			
Luis Juan B. Oreta Managing Director			
CEO & 15 Most Highly Compensated Executive Officers	Actual 2006 (restated)	₱164.62 M	₱226.94 M
	Actual 2007	₱176.07 M	₱122.45 M
	Projected 2008	₱193.68 M	₱44.73 M ***
All other officers**** as a group unnamed	Actual 2006 (restated)	₱228.06 M	₱363.51 M
	Actual 2007	₱233.84 M	₱153.60 M
	Projected 2008	₱257.22 M	₱58.57 M ***

\* Retired effective 30 June 2007

\*\* Retired effective 31 December 2007

\*\*\* Composed of guaranteed and performance bonus provision

\*\*\*\* Managers and up (including all above-named Officers)

The total annual compensation includes basic pay and other taxable income (guaranteed bonus, performance-based incentive and exercise of Stock Option).

The Company has no other arrangement with regard to the remuneration of its existing directors and officers aside from the compensation received as herein stated.

b. **Compensation of Directors**

Article IV Section 21 of the Company's By-Laws provides:

“Section 21 - The members of the Board of Directors of the Corporation who are neither officers nor consultants of the Corporation shall be entitled to a director's fee in an amount to be fixed by the stockholders at a regular or special meeting duly called for the purpose.”

i. **Standard Arrangement**

During the 2003 Annual Stockholders' Meeting, the stockholders ratified the resolution fixing the remuneration of non-executive directors at ₱1,000,000.00 consisting of the following components:

Retainer Fee:	₱500,000.00
Per diem per Board meeting attended:	₱100,000.00

In addition, a non-executive director is entitled to a per diem of ₱20,000.00 per board committee meeting actually attended.

ii. **Other Arrangement**

None of the directors, in their personal capacity, has been contracted and compensated by the Company for services other than those provided as a director.

The Company has no other arrangement with regard to the remuneration of its existing directors and officers aside from the compensation received as herein stated.

c. **Employment Contracts and Termination of Employment and Change-in-Control Arrangements**

The above named executive officers are covered by Letters of Appointment with the Company stating therein their respective job functionalities, among others.

d. **Warrants and Options Outstanding: Repricing**

- i. The Company offered the Executive Stock Option Plan (ESOP) to the Company's officers since 1995. Of the above named officers, there were 72,636 common shares exercised for the year 2007 by the following officers, to wit:

Name	No. of Shares	Date of Grant	Exercise Price	Market Price at Date of Grant
Aristón Estrada, Jr.		Various	Various	Various
Solomon M. Hermosura		Various	Various	Various
Ricardo N. Jacinto		Various	Various	Various
Rufino Luis T. Manotok		Various	Various	Various
Rufino F. Melo III		Various	Various	Various
All above-named Officers as a group	72,636		166.68	236.71*

\* Average price at date of grant.

- ii. The Company has adjusted the exercise price and market price of the options awarded to the above named officers due to the stock dividend declared by the Company in May 2004 and June 2007 and to the reverse stock split in May 2005.

## **Item 7. Independent Public Accountants**

- a. The principal accountants and external auditors of the Company is the accounting firm of SyCip, Gorres, Velayo & Company (SGV & Co.). The same accounting firm is being recommended for re-election at the scheduled annual meeting.
- b. Representatives of SGV & Co. for the current year and for the most recently completed fiscal year are expected to be present at the Annual Stockholders' Meeting. They will have the opportunity to make a statement if they desire to do so and are expected to be available to respond to appropriate questions.

Pursuant to the General Requirements of SRC Rule 68, Par. 3 (Qualifications and Reports of Independent Auditors), the Company has engaged SGV & Co. as external auditor of the Company, and Ms. Lucy L. Chan has been the Partner In-charge effective audit year 2007.

c. **Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

The Company has engaged the services of SGV & Co. during the two most recent fiscal years. There are no disagreements with SGV & Co. on accounting and financial disclosure.

d. **Audit and Audit-Related Fees**

The Company paid or accrued the following fees, including VAT, to its external auditors in the past two years:

	<u>Audit &amp; Audit-related Fees</u>	<u>Tax Fees</u>	<u>Other Fees</u>
2007	₱ 3.00 M	-	₱ 0.39 M
2006	2.75 M	-	4.61 M

SGV & Co. was engaged by the Company to audit its annual financial statements.

e. **Tax Fees**

No consultancy services were secured from SGV & Co.

f. **All Other Fees**

In 2007, SGV & Co. rendered the PFRS Seminars to the Company for an aggregate fee of ₱0.39M.

In 2006, SGV & Co. billed the following services to the Company for an aggregate fee of ₱4.61M:

- Agreed-upon Procedures for the primary offer of Preferred “B” shares
- Business Process Review
- Business Continuity Plan Development

The Company’s Audit Committee (composed of Meneleo J. Carlos, Jr., Xavier P. Loinaz and Toshifumi Inami) recommended to the Board of Directors the appointment of SGV & Co. as its external auditor and the fixing of the audit fees. Likewise, the other services rendered by SGV & Co. were approved by the Board of Directors upon the recommendation of the Audit Committee. The stockholders further ratified the resolution of the Board of Directors.

## C. ISSUANCE AND EXCHANGE OF SECURITIES

### Item 8. Authorization or Issuance of Securities Other than for Exchange

#### Stock dividend on common shares

a. **Title and amount of securities to be issued**

Declaration of a 20% stock dividend to all common shareholders of the Company equivalent to approximately 83 Million common shares with a par value of Fifty Peso (₱50.00) per share.

b. **Description of securities**

The authorized capital stock of the Company is Thirty Seven Billion Pesos (₱37,000,000,000.00), Philippine Currency, consisting of Six Hundred Million (600,000,000) Common Shares with a par value of ₱50.00 per share, and One Billion Two Hundred Fifty Eight Million (1,258,000,000) Preferred Shares divided into Nine Hundred Million (900,000,000) Preferred “A” shares, Three Hundred Million (300,000,000) Preferred “AA” shares, both classes with a par value of ₱1.00 per share, and Fifty Eight Million (58,000,000) Preferred “B” Shares with a par value of ₱100.00 per share.

The Common Shares may be owned or subscribed by or transferred to any person, partnership, association or corporation regardless of nationality, provided that at anytime at least 60% of the outstanding capital stock shall be owned by citizens of the Philippines or by partnerships, associations or corporations 60% of the voting stock or voting power of which is owned and controlled by citizens of the Philippines.

Shares of common stock are entitled to vote and to dividends, and shall be subject to the stockholders' preemptive right in accordance with law subject to the provisions of the Amended Articles of Incorporation.

**c. Description of transaction in which the securities are to be issued**

- ii. No amount of consideration will be received by the Company in the declaration of the 20% stock dividend.
- iii. The resolution of the Board of Directors adopted on 31 January 2008, approving the declaration of a 20% stock dividend to all the common shareholders of the Company, will be presented at the annual stockholders' meeting for the ratification of stockholders representing at least 2/3 of the outstanding capital stock entitled to vote.

**d. Reason for the proposed issuance**

The Company has historically declared dividends to its stockholders pursuant to the Company's dividend policy.

*New Preferred "A" Shares*

**a. Title and amount of securities to be issued**

Re-issuance of 12 Million new Preferred "A" shares with a par value of ₱100.00 per share as and when approved by the Securities and Exchange Commission.

**b. Description of securities**

Shares of preferred stock are entitled to dividends and are non-voting, non-convertible into common shares and have no preemptive rights to any issue of shares, common or preferred.

**c. Description of transaction in which the securities are to be issued**

- i. Currently, there is no transaction that will require immediate issuance of the Shares. All terms and conditions concerning the issuance of the Shares in the future shall be approved by the Board of Directors of the Company.
- ii. The resolutions of the Board of Directors adopted on 31 January 2008, approving the re-issuance and reclassification of the redeemed 1.2 Billion Preferred "A" and "AA" Shares with a par value of ₱1.00 per share into 12 Million new Preferred "A" Shares with a par value of ₱100.00 per share, and the amendment of the Amended Articles of Incorporation of the Company to reflect the same, will be presented at the annual stockholders' meeting for the ratification of the stockholders representing at least 2/3 of the outstanding capital stock entitled to vote.

**d. Reason for the proposed issuance**

The re-issuance of the new Preferred "A" Shares may be used to refinance debt.

- e. There are no provisions in the Company's Articles of Incorporation or By-laws that would delay, defer or prevent a change in control of the Company.

## **Item 9. Modification or Exchange of Securities**

The re-issuance and reclassification of the redeemed 1.2 Billion Preferred “A” and “AA” Shares with a par value of ₱1.00 per share into 12 Million new Preferred “A” Shares with a par value of ₱100.00 per share, will be presented at the annual stockholders’ meeting for the ratification of the stockholders.

The future issuance of the preferred shares may be used to raise corporate funds.

The essential features of the new Preferred “A” Shares will have the same features as the outstanding Preferred “B” Shares of the Company.

## **Item 10. Financial and Other Information**

The audited financial statements as of 31 December 2007, Management’s Discussion and Analysis, Market Price of Shares and Dividends and other data related to the Company’s financial information are attached hereto as Annex “B”. The Schedules required under Part IV(c) of Rule 68 will be included in the Annual Report (Form 17-A).

## **Item 11. Mergers, Consolidations, Acquisitions and Similar Matters**

There are no matters or actions to be taken up in the meeting with respect to merger, consolidation, acquisition by, sale or liquidation of the Company.

## **Item 12. Acquisition or Disposition of Property**

There are no matters or actions to be taken up in the meeting with respect to acquisition or disposition of any property by the Company.

## **Item 13. Restatement of Accounts**

### Changes in Accounting Policies

The accounting policies adopted are consistent with those of the previous financial year except as follows:

#### *Amendments to PFRSs and Philippine Interpretations effective in 2007*

The Group has adopted the following new and amended PFRS and Philippine Interpretations during the year.

- PFRS 7, *Financial Instruments: Disclosures*
- PAS 1 Amendment - *Presentation of Financial Statements*
- Philippine Interpretation IFRIC 10, *Interim Financial Reporting and Impairment*

The principal effects of these changes are as follows:

#### *PFRS 7, Financial Instruments: Disclosures*

PFRS 7 introduces new disclosures to improve the information about financial instruments. It requires the disclosure of qualitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk, including sensitivity analysis to market risk. It replaces disclosure requirements in PAS 32, *Financial Instruments: Disclosure and Presentation* and PAS 30, *Disclosure in the Financial Statements of Banks and Similar Financial Institutions*. It is applicable to all entities that report under PFRS.

The Ayala Group of Companies (the “Group”) adopted the amendment to the transitional provisions of PFRS 7, as approved by the Financial Reporting Standards Council of the Philippines, which gives transitory relief with respect to the presentation of comparative information for the new risk disclosures about the nature and extent of risks arising from financial instruments. Accordingly, the Group does not need to present comparative

information for the disclosures required by paragraphs 31-42 of PFRS 7, unless the disclosure was previously required under PAS 32. Adoption of PFRS 7 resulted in additional disclosures, which are included throughout the financial statements. These disclosures include presenting the different classes of loans and receivables, roll forward of allowance for impairment losses, credit quality of financial assets, aging of past due but not impaired financial assets, and sensitivity analysis as to changes in interest and foreign exchange rates.

#### *PAS 1 Amendment - Presentation of Financial Statements*

The amendment to PAS 1 introduces disclosures about the level of an entity's capital and how it manages capital.

#### *Philippine Interpretation IFRIC 10, Interim Financial Reporting and Impairment (effective for annual periods beginning on or after 01 November 2006)*

The Group adopted the Interpretation beginning 01 January 2007, which prohibits the reversal of impairment losses on goodwill and AFS equity investments recognized in the interim financial reports even if impairment is no longer present at the annual balance sheet date. Adoption of the Interpretation did not have any significant impact on the consolidated financial statements.

#### Future Changes in Accounting Policies

The Group has not applied the following new and amended PFRS and Philippine Interpretations which are not yet effective for the year ended 31 December 2007:

- *PFRS 8, Operating Segments (effective for annual periods beginning on or after 01 January 2009).*  
PFRS 8 requires a management approach to reporting segment information. PFRS 8 will replace PAS 14, *Segment Reporting*, and is required to be adopted only by entities whose debt or equity instruments are publicly traded, or are in the process of filing with the Securities and Exchange Commission (SEC) for purposes of issuing any class of instruments in a public market. The Group will apply PFRS 8 in 2009 and will assess the impact of this standard on its current manner of reporting segment information.
- *PAS 1, Presentation of Financial Statements (Revised) (effective for annual periods beginning on or after 01 January 2009)*  
The revised standard requires that the statement of changes in equity includes only transactions with owners and all non-owner changes are presented in equity as a single line with details included in a separate statement. Owners are defined as holders of instruments classified as equity.

In addition, the amendment to PAS 1 provides for the introduction of a new statement of comprehensive income that combines all items of income and expense recognized in the statements of income together with 'other comprehensive income'. The revisions specify what is included in other comprehensive income, such as gains and losses on available-for-sale assets, actuarial gains and losses on defined benefit pension plans and changes in the asset revaluation reserve. Entities can choose to present all items in one statement, or to present two linked statements, a separate statement of income and a statement of comprehensive income. The Group will assess the impact of the standard on its current manner of reporting all items of income and expenses.

- *PAS 23 Amendment - Borrowing Costs (effective for annual periods beginning on or after 01 January 2009)*  
The standard has been amended to require capitalization of borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset. A qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale. In accordance with the transitional requirements in the amendment, this change in accounting for borrowing costs shall be accounted for prospectively. Accordingly, borrowing costs will be capitalized on qualifying assets with a commencement date after 01 January 2009. No changes will be made for borrowing costs incurred to this date that have been expensed. The Group does not expect that the adoption of this Standard will have a significant impact on the consolidated financial statements.

- Philippine Interpretation IFRIC 11, *PFRS 2, Group and Treasury Share Transactions (effective for annual periods beginning on or after 01 March 2007)*.

This Interpretation requires arrangements whereby an employee is granted rights to an entity's equity instruments to be accounted for as an equity-settled scheme by the entity even if the entity chooses or is required to buy those equity instruments (e.g., treasury shares) from another party, or the shareholder(s) of the entity provide the equity instruments needed. It also provides guidance on how subsidiaries, in their separate financial statements, account for such schemes when their employees receive rights to the equity instruments of the parent. The Group does not expect this interpretation to have a significant impact on the consolidated financial statements.

- Philippine Interpretation IFRIC 12, *Service Concession Arrangements (effective for annual periods beginning on or after 01 January 2008)*.

This Interpretation applies to service concession operators and explains how to account for the obligations undertaken and rights received in service concession arrangements. The Interpretation prescribes the accounting for the rights which the Operator receives from the Grantor using either:

- Financial asset model wherein the Operator shall recognize a financial asset to the extent that it has an unconditional contractual right to receive cash from the Grantor.

The Operator has an unconditional right to receive cash if the Grantor contractually guarantees to pay the Operator;

- Intangible asset model wherein the Operator shall recognize an intangible asset to the extent that it receives a right to charge the users (not an unconditional right to receive cash because the amounts are contingent on the extent that the public uses the service);

- Mixed model if the Operator is paid by the users, but the Grantor guarantees a certain minimum amount to be paid to the Operator, the Financial Asset Model is used to the extent of such amount.

Manila Water Company, Inc. is currently assessing the impact of the adoption of this standard.

- Philippine Interpretation IFRIC 13, *Customer Loyalty Programmes (effective for annual periods beginning on or after 01 July 2008)*.

This Interpretation requires customer loyalty award credits to be accounted for as a separate component of the sales transaction in which they are granted and therefore part of the fair value of the consideration received is allocated to the awards credits and deferred over the period that the award credits are fulfilled. The Group does not expect this Interpretation to have a significant impact on the consolidated financial statements as no such scheme currently exists.

- Philippine Interpretation IFRIC 14, *PAS 19 - Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction (effective for annual periods beginning on or after 01 January 2008)*.

This Interpretation provides guidance on how to assess the limit on the amount of surplus in a defined benefit scheme that can be recognized as an asset under PAS 19, *Employee Benefits*. It also explains how the pension asset or liability may be affected by a statutory or contractual minimum funding requirement. The Group does not expect this Interpretation to have a significant impact on the consolidated financial statements.

## **D. OTHER MATTERS**

### **Item 14. Action with Respect to Reports**

- a. Approval of the Minutes of the 2007 Annual Meeting of the Stockholders held on 30 March 2007 covering the following matters:
  - i) Annual Report of Officers;
  - ii) Ratification and approval of all acts and resolutions of the Board of Directors and the Executive

- Committee for the fiscal year 2006;
  - iii) Ratification of the Resolution of the Board of Directors declaring a 20% Stock Dividend and approving the increase in authorized capital stock from ₱26B to ₱37B, and the amendment of Article Seventh of the Amended Articles of Incorporation to reflect the capital increase;
  - iv) Ratification of the merger into Ayala Corporation of its wholly-owned subsidiary, PFC Properties, Inc.;
  - v) Election of the Members of the Board of Directors, including the Independent Directors, and
  - vi) Election of External Auditors and Fixing their Remuneration.
- b. Approval of the Annual Report of Management for the year ending 31 December 2007.

### **Item 15. Matters not required to be Submitted**

All matters or actions to be submitted in the meeting will require the vote of the security holders.

### **Item 16. Amendment of Charter, By-laws or Other Documents**

Upon ratification by the stockholders, the Amended Articles of Incorporation of the Company will be further amended to reflect the reclassification of the redeemed 1.2 Billion Preferred "A" and "AA" Shares with a par value of ₱1.00 per share into 12 Million new Preferred "A" Shares with a par value of ₱100.00 per share.

### **Item 17. Other Proposed Actions**

- a. Ratification of all acts and resolutions of the Board of Directors and Management for the period covering 01 January 2007 through 31 December 2007 adopted in the ordinary course of business involving:
  - i) Approval of investments;
  - ii) Treasury matters including borrowings, opening of accounts and bank transactions;
  - iii) Appointment of signatories and amendments thereof;
- b. Ratification of the Resolutions of the Board of Directors adopted on 31 January 2008:
  - i) declaring a 20% Stock Dividend to all holders of common shares of the Company as of a record date to be fixed during the annual stockholders' meeting
  - ii) re-issuance and reclassification of the redeemed 1.2 Billion Preferred "A" and "AA" Shares with a par value of ₱1.00 per share into 12 Million new Preferred "A" Shares with a par value of ₱100.00 per share, and the amendment of Article Seventh of the Amended Articles of Incorporation to reflect the same;
- c. Election of the Members of the Board of Directors, including the Independent Director, for the ensuing calendar year.
- d. Election of External Auditors and fixing their remuneration.

### **Item 18. Voting Procedures**

- a. **Vote required:** The vote of stockholders representing at least two-thirds (2/3) of the issued and outstanding capital stock entitled to vote is required.
- b. **Method of Voting:** Straight and Cumulative Voting

In all items for approval except election of directors, each share of stock entitles its registered owner to one vote.

In case of election of directors, each common stockholder may vote such number of shares for as many persons as there are directors to be elected or he may cumulate said shares and give one nominee as many votes as the number of directors to be elected multiplied by the number of his shares shall equal, or he may distribute them on the same principle among as many nominees as he shall see fit, provided that the whole

number of votes cast by him shall not exceed the number of shares owned by him multiplied by the total number of directors to be elected.

If there are more than seven nominees for the 7-member Board of Directors, voting shall be done by secret ballot. If there are only seven nominees, voting will be done by show of hands.

The external auditor of the Company, SGV & Co., will validate the ballots when voting is done by secret ballot. Likewise, SGV & Co. will count the number of hands raised when voting by show of hands is done.

**After reasonable inquiry and to the best of my knowledge and belief, I certify that the information set forth in this report is true, complete and correct. This report is signed in the City of Makati on the 27<sup>th</sup> day of February 2008.**

**AYALA CORPORATION**



by: **MERCEDITA S. NOLLEDO**  
Corporate Secretary

**ANNEX “A”**  
**DIRECTORS AND KEY OFFICERS**

The write-ups below include positions currently held by the directors and executive officers, as well as positions held during the past five years.

**Board of Directors**

Jaime Augusto Zobel de Ayala	Chairman and Chief Executive Officer
Fernando Zobel de Ayala	President and Chief Operating Officer
Meneleo J. Carlos, Jr.	Independent Director
Toshifumi Inami	Director
Delfin L. Lazaro	Director
Xavier P. Loinaz	Director
Mercedita S. Nolleddo	Director

***Jaime Augusto Zobel de Ayala***, Filipino, 48, has served as Director of Ayala Corporation since 1987. He also holds the following positions: Chairman and CEO and Chairman of the Nomination Committee of Ayala Corporation; Chairman of the Board of Directors of Globe Telecom, Inc., Bank of the Philippine Islands and Integrated Micro-electronics, Inc.; and Director of Ayala Land, Inc. He is a member of various international and local business and socio-civic organizations including the JP Morgan International Council, Mitsubishi Corporation International Advisory Committee, Toshiba International Advisory Group, Harvard University Asia Center Advisory Committee, Board of Trustees of the Asian Institute of Management and a national council member of the World Wildlife Fund (US). He was a TOYM (Ten Outstanding Young Men) Awardee in 1999 and was named Management Man of the Year in 2006 by the Management Association of the Philippines for his important role in the transformation of Ayala Corporation into a highly diversified forward-looking conglomerate. He was also awarded the prestigious Harvard Business School Alumni Achievement Award in 2007. He graduated with B.A. in Economics (Cum Laude) at Harvard College in 1981 and took his MBA (with Distinction) at the Harvard Graduate School of Business Administration in 1987.

***Fernando Zobel de Ayala***, Filipino, 47, has served as Director of Ayala Corporation since 1994. He also holds the following positions: President and Chief Operating Officer of Ayala Corporation; Chairman of Ayala Land, Inc., Manila Water Company, Inc., AC International Finance Ltd., Ayala International Pte. Ltd., Ayala Automotive Holdings Corp., Ayala Hotels, Inc., Alabang Commercial Corp., and Anvaya Cove Beach and Nature Club, Inc.; Co-Vice Chairman and Trustee of Ayala Foundation, Inc.; Director of the Bank of the Philippine Islands, Globe Telecom, Inc., Integrated Micro-electronics Inc., AI North America and Habitat for Humanity International; and Member of the East Asia Council of INSEAD. He graduated with B.A. Liberal Arts at Harvard College in 1982.

***Meneleo J. Carlos, Jr.***, Filipino, 78, serves as the Independent Director of Ayala Corporation since September 2002. He is the Chairman of Ayala Corporation’s Audit and Compensation Committees and a member of the Nomination Committee. He is the Chairman and President of RI Chemical Corporation; President of Resins, Inc., Riverbanks Development Corporation; Chairman of the Federation of Philippine Industries, Maja Development Corporation, AVC Chemical Corporation, Philippine Iron Construction & Marine Works, Inc. (PICMW) and Vacphil Rubber Corporation; and Director of Philippine Aerosol Container Corp. (PACC) and Cagayan Electric Power & Light Company (CEPALCO). He graduated with a B.S. Chemical Engineering degree and a Certificate of Advanced Studies at Cornell University in 1952.

***Toshifumi Inami***, Japanese, 56, has served as Director of Ayala Corporation since June 2006. He is currently the General Manager of Mitsubishi Corporation-Manila Branch and Senior Vice President of Mitsubishi Corporation-Tokyo, Japan. He is the Chairman of International Elevator & Equipment, Inc.; Chairman and President of MCPL (Philippines), Inc.; Director in the following companies: The Japanese Association Manila, Inc., Isuzu Philippines Corp., MD Distripark Manila, Inc., MD Laguna Corporation, Imasen Philippines Manufacturing Corp., Kansai Paint Philippines, Trans World Agro-Products Corporation, Kepco Ilijan Corporation, Team Energy and UniCharm Philippines Inc.; and President of Japanese Chamber of Commerce & Industry of the Philippines (JCCPI). Prior to his assignment at Mitsubishi Corporation-Manila Branch, he was the General Manager at the Ship Department of

Mitsubishi Corporation-Tokyo, Japan. Mr. Inami had a degree in BS Mechanical Engineering from Keio University in Japan.

**Delfin L. Lazaro**, Filipino, 61, was elected to the Board of Ayala on 01 January 2007. He has served as a member of the Management Committee of Ayala Corporation (Ayala Group) since 1996. He also holds the following positions: Director and Chairman of the Executive Committee of Globe Telecom, Inc.; Chairman of Ayala Systems Technology, Inc., HRMall, Inc. and Atlas Fertilizer & Chemicals; Director of Ayala Land, Inc., Integrated Micro-electronics, Inc., Manila Water Co., Inc., AI North America, Inc., Ayala International Holdings, Ltd. and Ayala Automotive Holdings Corp. Formerly, Mr. Lazaro was the President and CEO of Benguet Corporation and Secretary of the Department of Energy of the Philippine government. He was named Management Man of the Year 1999 by the Management Association of the Philippines for his contribution to the conceptualization and implementation of the Philippine Energy Development Plan and to the passage of the law creating the Department of Energy. He was also cited for stabilizing the power situation that helped the country achieve successively high growth levels up to the Asian crisis in 1997. He graduated with BS Metallurgical Engineering at the University of the Philippines in 1967 and took his MBA (with Distinction) at Harvard Graduate School of Business in 1971.

**Xavier P. Loinaz**, Filipino, 64, has served as director of Ayala Corporation since April 2006. He was a member of the Management Committee of Ayala Corporation (Ayala Group) from 1989 to 2004. He was formerly the President of Bank of the Philippine Islands (BPI) from 1982 to 2004. Other positions held are: Director of BPI, BPI Capital Corporation, BPI Direct Savings Bank, Inc., BPI/MS Insurance Corporation, BPI Family Savings Bank, Inc. and Chairman of the Board of Directors of Ayala Life Assurance, Inc.; and Member of the Board of Trustees of BPI Foundation, Inc. He graduated with an AB Economics degree at Ateneo de Manila University in 1963 and took his MBA-Finance at Wharton School, University of Pennsylvania in 1965.

**Mercedita S. Nollo**, Filipino, 66, has served as Director of Ayala Corporation since 2004 and is also a Senior Managing Director and Corporate Secretary of Ayala Corporation, and Senior Counsel of the Ayala Group of Companies. Her other significant positions include: Director and Corporate Secretary of Ayala Land, Inc.; Director of Honda Cars Cebu, Inc., Honda Cars Makati, Inc., Isuzu Automotive Dealership, Inc., Isuzu Cebu, Inc., Ayala Automotive Holdings Corp., Bank of the Philippine Islands, BPI Family Bank, BPI Capital Corp. and Anvaya Cove Beach and Nature Club, Inc.; Corporate Secretary and Member of the Board of Trustees of Ayala Foundation, Inc.; Director and Treasurer of Phil. Tuberculosis Society, Inc. She had her education at the University of the Philippines and graduated Magna Cum Laude and Class Valedictorian in Bachelor of Science in Business Administration and Cum Laude and Class Valedictorian in Bachelor of Laws.

#### **Management Committee Members / Key Executive Officers**

* Jaime Augusto Zobel de Ayala	Chairman & Chief Executive Officer
* Fernando Zobel de Ayala	President & Chief Operating Officer
* Delfin L. Lazaro	
* Mercedita S. Nollo	Senior Managing Director, Senior Counsel & Corporate Secretary
** Gerardo C. Ablaza, Jr.	Senior Managing Director
** Antonino T. Aquino	Senior Managing Director
** Jaime I. Ayala	Senior Managing Director
** Charles H. Cosgrove	Senior Managing Director
** Rufino Luis T. Manotok	Senior Managing Director, Corporate Information Officer & Chief Finance Officer
** Arthur R. Tan	Senior Managing Director
** Victoria P. Garchitorena	Managing Director
** Aurelio R. Montinola III	
** Renato O. Marzan	Managing Director, General Counsel, Assistant Corporate Secretary & Compliance Officer
Ramon G. Opulencia	Managing Director & Treasurer
** John Philip S. Orbeta	Managing Director
* Members of the Board of Directors	
** Management Committee members	

**Gerardo C. Ablaza, Jr.**, Filipino, 54, has served as a member of the Management Committee of Ayala Corporation (Ayala Group) since 1998. He also holds the following positions: Senior Managing Director of Ayala Corporation and President and CEO of Globe Telecom, Inc. He was previously Vice President and Country Business Manager

for the Philippines and Guam of Citibank, N.A. for its Global Consumer Banking business. Prior to this position, he was Vice President of Citibank, N.A. Singapore for Consumer Banking. Attendant to his last position in Citibank, N.A., he was the bank's representative to the Board of Directors of CityTrust Banking Corporation and its various subsidiaries. He graduated Summa Cum Laude at De La Salle University in 1974 with a degree in AB Major in Mathematics (Honors Program).

**Antonino T. Aquino**, Filipino, 60, has served as a member of the Management Committee of Ayala Corporation (Ayala Group) since August 1998. He also holds the following positions: Managing Director of Ayala Corporation and President of Manila Water Company, Inc. He also served as President of Ayala Property Management Corporation, Senior Vice President of Ayala Land, Inc., and a Business Unit Manager in IBM Philippines, Inc. He graduated with Bachelor of Science Major in Management at the Ateneo de Manila University in 1968 and has completed academic units for the Masteral Degree in Business Management at the Ateneo Graduate School of Business in 1975.

**Jaime I. Ayala**, Filipino, 45, has served as a member of the Management Committee of Ayala Corporation (Ayala Group) since 2004. He also holds the following positions: Senior Managing Director of Ayala Corporation and President and CEO of Ayala Land, Inc. His other significant positions include: Chairman of the Board of Directors and President of Makati Property Ventures, Inc.; Chairman of the Board of Directors of Ayala Property Management Corp., Cebu Holdings, Inc., Cebu Insular Hotel Co., Inc., Cebu Property Ventures & Dev't. Corp., Community Innovations, Inc., Avida Land Corp., Laguna Technopark, Inc., Makati Development Corp., and Station Square East Commercial Corp; Member of the Board of Directors and President of Aurora Properties, Inc, Ayala Hotels, Inc., Ceci Realty Inc., Enjay Hotels, Inc., Roxas Land Corp., Vesta Property Holdings, Inc. and Anvaya Cove Beach and Nature Club, Inc.; Member of the Board of Directors of Alabang Commercial Corp., Ayala Greenfield Development Corp., Ayala Infrastructure Ventures, Inc., Ayala Land Sales, Inc., Berkshire Holdings, Inc., Bonifacio Arts Foundation, Inc., Bonifacio Land Corp., Emerging City Holdings, Inc., Fort Bonifacio Development Corp., myAyala.com, Inc., Ayala Center Association and Makati Parking Authority. Prior to joining ALLI, he spent 19 years with McKinsey & Company in the US, Mexico, Tokyo and Hong Kong. At McKinsey, he was a Director (senior partner) and played a number of global and regional leadership roles, including that of President of McKinsey's Manila office. He earned his M.B.A. from Harvard School, graduating with honors in 1988. He completed his undergraduate work in 1984 at Princeton University, where he graduated Magna Cum Laude in Economics, with a minor in Engineering.

**Charles H. Cosgrove**, American, 52, has served as a member of the Management Committee of Ayala Corporation (Ayala Group) since 1998. He is also a Senior Managing Director of Ayala Corporation and CEO of AG Holdings Ltd. Prior to joining Ayala Corporation, he was a Managing Director of Singapore Telecom International Pte. Ltd. He graduated from Stanford University with an AB in 1977. He obtained a JD from Georgetown University School of Law in 1980.

**Rufino Luis T. Manotok**, Filipino, 57, has served as a member of the Management Committee of Ayala Corporation (Ayala Group) since 1999. He also holds the following positions: Senior Managing Director, Corporate Information Officer and Chief Finance Officer of Ayala Corporation; President and Chairman of the Board of Directors of Honda Cars Makati, Inc., Isuzu Automotive Dealership, Inc., Isuzu Iloilo Corp. and Honda Cars Cebu, Inc.; Chairman of Isuzu Cebu, Inc.; President and Director of Ayala Automotive Holdings Corp., Philwater Holdings Company and Ayala Aviation Corp.; and Director of AC International Finance Ltd., AI North America, Inc., Asiacom Philippines, Inc., AYC Holdings Ltd., Ayala Systems Technology, Inc., BPI Family Savings Bank, Inc., and Michigan Holdings, Inc. He graduated with Bachelor of Arts in Economics at the Ateneo de Manila University in 1971 and had his Masters Degree in Business Management at the Asian Institute of Management in 1973. He also took the Advance Management Program at Harvard Business School in 1994.

**Arthur R. Tan**, Filipino, 48, has served as a member of the Management Committee of Ayala Corporation (Ayala Group) for more than 5 years. He holds the position of Senior Managing Director of Ayala Corporation. He is also the President and CEO of Integrated Micro-electronics, Inc., and Speedy-Tech Electronics, Ltd. and Chairman of the Board of Speedy-Tech Philippines, Inc. Prior to joining Ayala Corporation, he was a Managing Director of American Microsystems, Inc. (Asia Pacific Region/Japan). He graduated with a degree of BS in Electronics and Communication Engineering at the Mapua Institute of Technology in 1982. He has taken post graduate classes in MSEE from the University of Idaho and business courses from Harvard University.

**Victoria P. Garchitorea**, Filipino, 63, has served as a member of the Management Committee of Ayala Corporation (Ayala Group) since 2006. She is currently the Managing Director of Ayala Corporation (since 1996), President and Board member of Ayala Foundation, Inc. and Ayala Foundation USA. Her other significant positions include: Trustee of the International Center on Innovation, Transformation and Excellence in Governance and Pinoy Me Foundation; Governor of Management Association of the Philippines; member of the Asia Pacific Advisory Council Against Corruption-World Bank and Makati Business Club; and member of the National Committee of Bishops-Businessmen's Council for Human Development. Previously, she was a Senior Consultant on Poverty Alleviation and Good Governance and the Head of the Presidential Management Staff and Secretary to the Cabinet under the Office of the President of the Republic of the Philippines; a Director of Philippine Charity Sweepstakes Office; Executive Assistant to the Chairman and President of the Meralco Foundation, Inc.; a Trustee of the Ramon Magsaysay Awards Foundation; and Co-Chairperson of EDSA People Power Commission. She graduated with a B.S. Physics degree (Summa Cum Laude) at the College of the Holy Spirit in 1964 and was an SGV scholar at the Asian Institute of Management.

**Aurelio R. Montinola III**, Filipino, 56, has served as member of the Management Committee of Ayala Corporation (Ayala Group) since 2005. He also holds the following positions: President and CEO of the Bank of the Philippine Islands; Vice Chairman of the Board of Directors of Republic Cement Corporation; Vice Chairman of the Board of Trustees of Far Eastern University; Chairman of East Asia Educational Foundation, Inc.; Chairman of the Board of Directors of Amon Trading Corporation; Regional Board of Advisers of MasterCard Incorporated; Director of Ayala Land, Inc., Manila Water Company, Inc.; President of BPI Foundation, Inc.; Director of Makati Business Club; and Member of Management Association of the Philippines. He graduated with a degree in BS Management Engineering at the Ateneo de Manila University in 1973 and received his MBA at Harvard Business School in 1977.

**Renato O. Marzan**, Filipino, 59, has served as a member of the Management Committee of Ayala Corporation (Holding Company) since May 2007. He also holds the following positions: General Counsel, Managing Director, Compliance Officer and Assistant Corporate Secretary of Ayala Corporation; Director and Corporate Secretary of Integrated Micro-electronics, Inc., Honda Cars Makati, Inc., and Isuzu Automotive Dealership, Inc.; Corporate Secretary of Globe Telecom, Inc., AC International Finance Ltd., Cebu Holdings, Inc., Cebu Property Ventures and Development Corp., Avida Land, Corp., Ayala Hotels, Inc., Alabang Commercial Corp., Community Innovations, Inc., and Ayala Automotive Holdings Corporation; and Assistant Corporate Secretary of Ayala Land, Inc. and Ayala Foundation, Inc. He had his education at the San Beda College with a degree in Bachelor of Arts in Philosophy (Magna Cum Laude) in 1969 and Bachelor of Laws (Cum Laude) in 1973.

**Ramon G. Opulencia**, Filipino, 51, has served as Treasurer of Ayala Corporation since September 2005 and has previously served as the Senior Assistant Treasurer from November 1992 to September 2005. He is also a Managing Director of Ayala Corporation. He is currently a member of the Board of Directors and the Audit Committee of BPI Family Savings Bank, Inc. Prior to joining Ayala Corporation, he was a Senior Manager of the Bank of the Philippine Islands' Treasury Group. He graduated with a BS in Mechanical Engineering degree at the De La Salle University in 1978 and took his Masteral in Business Management at the Asian Institute of Management graduating with Distinction in 1983. He completed the Advanced Management Program at the Harvard Business School in May 2005.

**John Philip S. Orbeta**, Filipino, 46, has served as a member of the Management Committee of Ayala Corporation (Holding Company) since 2005. He is currently the Managing Director and Group Head for Corporate Resources, which includes Strategic Human Resources, Corporate Communications and Information & Communications Technology at Ayala Corporation. He is concurrently the Chairman of the Ayala Group Human Resources Council which brings together the Human Resources professionals from all the Ayala Group of Companies. He joined the Ayala Corporation in May of 2005 as Managing Director and Head of Strategic Human Resources and Organization Development and was concurrently the Senior Vice President and Head of the Human Resources Group of Ayala Land, Inc. Prior to joining Ayala Corporation, he spent 19 years at Watson Wyatt Worldwide (NYSE:WW), the global management consulting firm where he was the Vice President and Global Practice Director for the firm's Human Capital Consulting Group, overseeing the firm's practices in executive compensation, strategic rewards, data services and organization effectiveness around the world. He was also a member of Watson Wyatt's Board of Directors. He received his undergraduate degree in Economics from the Ateneo de Manila University where he also attended graduate studies in Industrial Psychology. He completed a Leadership Development Program at the Harvard Business School.

## ANNEX “B”

### I. MANAGEMENT’S DISCUSSION AND ANALYSIS (MD&A) OF FINANCIAL CONDITION AND RESULTS OF OPERATION

#### 2007

Ayala Corporation posted record consolidated revenues and net income in 2007. Despite the uncertainties looming in global financial markets in the latter part of the year, the domestic operating environment remained generally positive with economic fundamentals largely remaining intact. The main drivers of domestic consumption, particularly the robust overseas workers’ remittances, low domestic interest rate, revival of sectors like power and infrastructure as well as greater activity across several industries continued to underpin the growth of the Ayala group’s major businesses, particularly in property, telecom, banking, water, and automotive. However, the peso’s continued strength has also impacted the export-oriented businesses in the portfolio, particularly in the electronics and business process outsourcing services. But overall, the company’s growth momentum remained solid this year as the company also realized values from its portfolio and as operating units achieved generally higher earnings.

Consolidated revenues reached ₱78.7 billion, up 12% versus the prior year driven by a healthy growth in consolidated sales and services, higher equity in net earnings, interest income, and gains from the sale of shares particularly at the parent level.

Consolidated sales and services increased by 6% to ₱56.6 billion due mainly to higher unit sales of Ayala Automotive, higher contribution from the newly acquired companies of the electronics business as well as the new investments in business process outsourcing (BPO) under LiveIt. Growth, however, was partly weighed by the marginal revenue growth of the real estate group. While underlying demand across all of the company’s real estate products remained strong as reflected in strong residential unit sales and high occupancy rates of its commercial centers and business office portfolio, Ayala Land, Inc. (ALI) recorded only a slight revenue expansion as a result of the standardization of revenue recognition policy, which had the effect of accelerating its revenues in 2006. Sales and services accounted for 72% of total consolidated revenues in 2007.

Equity in net earnings of associates and joint ventures reflected an 18% increase to ₱9.7 billion from ₱8.2 billion in 2006. The strong earnings growth of the parent company’s key affiliates, particularly Globe Telecom, which posted a 13% growth in net income, banking unit, Bank of the Philippine Islands (BPI), which posted an 11% increase in net income, as well as the higher earnings of the associates of Ayala Land altogether resulted in higher equity earnings for the group. Equity earnings accounted for 12% of the company’s total revenues in 2007.

Consolidated revenues were further boosted by capital gains which pushed the Other Income account up by 53% to ₱10.7 billion. A substantial part of this was generated through value realization initiatives at the parent level as it recognized ₱7.3 billion in gains from the sale of shares in Ayala Land, BPI, and Globe as market values during the year reached attractive levels for value realization.

On the cost side, consolidated cost and expenses increased by 8% to ₱58.4 billion. A substantial part of this was due to a 6% increase of consolidated cost of sales and services to ₱43.2 billion, which was very much in line with the growth of consolidated sales and services.

General and administrative expenses (GAE), on the other hand, rose by 23% to ₱9.5 billion stemming from expenses related to capacity expansion initiatives and amortization expense of the new BPO businesses, higher manpower and technology integration-related expenses of the electronics group.

Other charges increased by 306% to ₱1.6 billion as a result of non-cash, non-operating charges from the impairment loss on goodwill of the electronics, information technology and business process outsourcing services group, particularly Affinity Express and partly Integreon.

Consolidated interest expense and other financing charges declined by 18% to ₱4.1 billion from ₱5 billion the prior year. This was due to a substantial reduction in average funding costs. At the holding company level in particular, the continued decline in domestic interest rates has helped reduce financing expense significantly. Financing expense at the holding company level reached ₱3 billion in 2007, 26% lower than the prior year. In 2007 the parent company pre-paid a total of P14 billion worth of debt that had an average cost of 11.8%. Refinancing with lower

cost debt has brought down the average cost of parent company's outstanding debt in 2007 to 7.4% from 9.5% the prior year. Net debt at the parent level has also been substantially reduced and is now down to ₱13.3 billion, putting parent level net debt-to-equity ratio even lower at 0.15 to 1 from 0.26 to 1 at the beginning of the year. Even on a consolidated basis, consolidated debt by year-end 2007 was lower at ₱50 billion. With cash, cash equivalents and short-term investments of ₱40.5 billion, consolidated net debt declined to ₱9.5 billion from ₱29.6 billion and consolidated net debt to equity ratio at 0.11 to 1 from 0.38 to 1. Total stockholders' equity by year-end reached ₱87.2 billion, up 13% from the prior year.

Altogether, these put consolidated net income in 2007 at ₱16.2 billion, which was a 33% increase from the ₱12.2 billion net income recorded in 2006 and the highest ever recorded by the company.

The healthy earnings growth and strong cash position of the parent company enabled it to further increase its dividend payout in 2007 with a total of ₱7.3 billion paid out to shareholders, more than double the amount the prior year. This is equivalent to 60% of prior year's net income, inclusive of the 20% stock dividend, and a dividend yield of 1.4% based on an average price of ₱558.50 per share. This combined with the 15.5% gain in the company's stock price during the year put total return to shareholders at 17% in 2007.

The company's total market capitalization by year end reached ₱234 billion and was ranked the second largest among companies listed in the Philippine Stock Exchange. However, collectively, the market capitalization of the five listed companies of the group accounted for about 27% of the Philippine Stock Exchange's composite index's total market capitalization.

#### **Key performance indicators of the Company and its significant subsidiaries**

The table sets forth the comparative key performance indicators of the Company and its material subsidiaries.

(Amounts in millions, except ratios)

<b><i>Ayala Corporation (Consolidated)</i></b>		
	<b><u>2007</u></b>	<b><u>2006</u></b>
Revenue	78,708	70,166
Net Income	16,198	12,177
Total Assets	196,419	182,332
Total Debt	50,032	52,881
Stockholders' Equity	87,176	77,136
Current Ratio <sup>1</sup>	1.92	1.70
Debt to Equity Ratio <sup>2</sup>	0.57	0.69

<b><i>Ayala Land, Inc.</i></b>		
	<b><u>2007</u></b>	<b><u>2006</u></b>
Revenue	25,707	25,559
Net Income	4,386	3,866
Total Assets	82,981	78,250
Total Debt	10,139	12,837
Stockholders' Equity	45,705	40,651
Current Ratio <sup>1</sup>	1.65	1.64
Debt to Equity Ratio <sup>2</sup>	0.22	0.32

**Integrated Micro-electronics, Inc.**

	<b><u>2007</u></b>	<b><u>2006</u></b>
Revenue	19,757	20,187
Net Income	1,632	1,779
Total Assets	12,424	13,917
Total Debt	2,901	4,411
Stockholders' Equity	6,492	6,455
Current Ratio <sup>1</sup>	1.70	1.69
Debt to Equity Ratio <sup>2</sup>	0.45	0.68

**Ayala Automotive Holdings Corporation**

	<b><u>2007</u></b>	<b><u>2006</u></b>
Revenue	12,238	9,179
Net Income	201	105
Total Assets	2,848	1,855
Total Debt	566	79
Stockholders' Equity	1,322	1,164
Current Ratio <sup>1</sup>	1.40	1.74
Debt to Equity Ratio <sup>2</sup>	0.43	0.07

<sup>1</sup> Current Assets/Current Liabilities

<sup>2</sup> Total Debt/Stockholders' Equity (Total Debt includes short-term debt, long-term debt, current portion of long-term debt, cumulative preferred shares (classified as liabilities))

The table sets forth the comparative key performance indicators of the Company and its material subsidiaries.

In general, the above key performance indicators were within targeted levels.

For the balance sheet items (current ratio and debt to equity ratios), the company aims to maintain for its current ratio not to be lower than 0.5:1 and for its debt to equity ratio not to exceed 3:1. The company and its subsidiaries' ratios are considered better than these levels as a result of prudent debt management policies.

There were no events that will trigger direct or contingent financial obligation that is material to the Company, including any default or acceleration of an obligation.

Likewise, there were no material off-balance sheet transactions, arrangements, obligations (including contingent obligations), and other relationships of the Company with unconsolidated entities or other persons created during the reporting period.

**Causes for any material changes  
(Increase or decrease of 5% or more in the financial statements)**

Balance Sheet items  
(31 December 2007 Vs 31 December 2006)

**Cash and cash equivalents – 81% increase from ₱20,391mln to ₱36,836mln**

Attributable to proceeds from sale of shares of stocks, increased collections and proceeds from the issuance of preferred shares by the real estate group. As a percentage to total assets, cash and cash equivalents increased from 11% to 19% as of 31 December 2006 and 31 December 2007, respectively.

Short-term investments – 26% increase from ₱2,928mln to ₱3,688mln

Mainly due to money market placements of the parent company and the real estate group's investment management account in 2007 partly offset by the lower money market placements of the real estate group. As a percentage to total assets, short-term investments remained at 2% of the total assets as of 31 December 2006 and 31 December 2007.

Inventories – 6% decrease from ₱9,392mln to ₱8,843mln

Largely due to sale of units at residential building and subdivision projects by the real estate group partly offset by higher vehicles inventory by the automotive group. As a percentage to total assets, inventories remained at 5% as of 31 December 2006 and 31 December 2007, respectively.

Other current assets – 22% decrease from ₱3,961mln to ₱3,098mln

Sale of marketable securities partly offset by higher prepaid expenses of the real estate group. As a percentage to total assets, other current assets remained at 2% as of 31 December 2006 and 31 December 2007, respectively.

Noncurrent assets held for sale – 100% decrease from ₱3,658mln to ₱0-

Due to sale of Oakwood by the real estate group and sale of investment in Hermill by the international group in 2007. This account is 2% of the total assets as of 31 December 2006.

Noncurrent accounts and notes receivable – 59% increase from ₱2,520mln to ₱4,010mln

Due to availment of longer payment terms and additional sales at new and existing projects by the real estate group. Noncurrent accounts and notes receivable slightly increased from 1% of the total assets as of 31 December 2006 to 2% as of 31 December 2007.

Investments in associates and joint ventures – 4% increase from ₱68,569,mln to ₱71,560mln

Investments in associates, joint ventures and others includes the Company's and its subsidiaries' investments in various affiliates which are being accounted for under the equity method. These associates are Bank of the Philippine Islands, Globe Telecom and Manila Water Corporation, among others.

The increase is largely due to the investment in a BPO company partly booked in 2006 under Investment in bonds and other securities account by the electronics, information technology and business process outsourcing services group and 2007 equity share in earnings of associates partly offset by the sale of shares and dividends received by the parent company, lower forex rate and return of investment by the international group. This account slightly decreased from 38% of the total assets as of 31 December 2006 to 36% as of 31 December 2007.

Investment in bonds and other securities – 28% decrease from ₱3,462mln to ₱2,493mln

Sale of marketable securities and reclassification of investments in a BPO company to Investments in Associates & Joint Ventures account partially offset by new investments and marked to market investments of the electronics, information technology, business process outsourcing services group. This account is 2% of the total assets as of 31 December 2006 and 1% as of 31 December 2007.

Property, plant and equipment – 6% decrease from ₱9,057mln to ₱8,493mln

Decrease due to lower forex rate, depreciation expense and business development costs charged to expense by electronics, information technology, business process outsourcing services group partly offset by the ongoing projects of the real estate group. As of 31 December 2006 and 31 December 2007, the group's property, plant and equipment account is at 5% and 4% of the total assets, respectively.

Deferred tax assets – 12% decrease from ₱1,124mln to ₱984mln

Due mainly to realization of unrealized financial gross profit of the real estate group. As of 31 December 2006 and 31 December 2007, the group's deferred tax asset is at 0.6% and 0.5% of the total assets, respectively.

Pension assets – 31% decrease from ₱203mln to ₱141mln

Decrease in pension assets of the electronics, information technology, business process outsourcing services group. This account remained at 0.1% of the total assets as of 31 December 2006 and 31 December 2007.

Intangible assets – 26% decrease from ₱4,430mln to ₱3,276mln

Due to lower peso exchange rate, amortization in 2007 and impairment of goodwill. As a percentage to total assets, this account remained at 2% as of 31 December 2006 and 31 December 2007.

Other noncurrent assets – 17% increase from ₱1,785mln to ₱2,087mln

Cost of various facilities advanced by the electronics, information technology, business process outsourcing services group which will be billed to its customers. As a percentage to total assets, this account remained at 1% as of 31 December 2006 and 31 December 2007.

Accounts payable and accrued expenses – 21% increase from ₱18,326mln to ₱22,261mln

Higher trade payables by the real estate group and higher inventory pull-outs by the automotive group. As of 31 December 2006 and 31 December 2007, this account is at 23% and 27% of the total liabilities, respectively.

Short-term debt – 5% increase from ₱2,504mln to ₱2,634mln

New loan availed by the automotive group partly offset by the payment of debt by the international and electronics, information technology and business process outsourcing services groups. As of 31 December 2006 and 31 December 2007, this account remained at 3% of the total liabilities.

Other current liabilities – 7% increase from ₱1,453mln to ₱1,550mln

Increase in customers' deposits by the real estate group. As a percentage to total liabilities, this account is at 2% as of 31 December 2006 and 31 December 2007.

Liabilities directly associated with noncurrent assets held for sale – 100% decrease from ₱469mln to ₱0-

Due to sale of assets previously booked as held for sale. As a percentage to total liabilities, this account is at 0.6% as of 31 December 2006.

Cumulative redeemable preferred shares – 100% decrease from ₱2,500mln to ₱0-mln

Redemption of preferred shares by the parent company. Cumulative redeemable preferred shares is 3% of the total liabilities as of 31 December 2006.

Deferred tax liabilities – 65% decrease from ₱444mln to ₱156mln

Primarily due to reduction in deferred tax liabilities of the real estate group. As a percentage to total liabilities, deferred tax liabilities is at 0.6% and 0.2% as of 31 December 2006 and 31 December 2007, respectively.

Pension liabilities – 9% increase from ₱488mln to ₱532mln

Increase in pension liabilities of the real estate group. This account remained at 1% of the total liabilities as of 31 December 2006 and 31 December 2007.

Other noncurrent liabilities – 11% increase from ₱6,141mln to ₱6,818mln

Mainly due to increase in buyers' and tenants' deposits of the real estate group. This account remained constant at 8% of the total liabilities as of 31 December 2006 and 31 December 2007.

Paid-up capital – 16% increase from ₱23,138mln to ₱26,855mln

Largely due to the 20% stock dividend.

Share-based payments – 8% increase from ₱558mln to ₱604mln

Increase in stock options granted.

Cumulative translation adjustment – 671% decrease from (₱298mln) to (₱2,297mln)

Mainly due to forex rate changes.

Retained earnings – 17% increase from ₱51,659mln to ₱60,461mln

Attributable to 2007 net income net of cash and stock dividends declared.

Net unrealized gain on available-for-sale financial assets – 18% decrease from ₱2,079mln to ₱1,712mln

Due to lower revaluation of investments in securities.

Treasury shares – 51,414% increase from ₱0.310mln to ₱160mln

Due to buy-back of shares.

Minority interest – 12% increase from ₱24,699mln to ₱27,609mln

Largely due to share of minority holders in 2007 net income and increased share due to reduced shareholdings by the equity holders of the parent.

Income Statement items

(YTD 31 December 2007 Vs YTD 31 December 2006)

Sales and services – 6% increase from ₱53,394mln to ₱56,578mln

Higher unit sales by the automotive group, higher sales volume of existing businesses and contributions from the operations of newly acquired companies by the electronics, information technology and business process outsourcing services group partly offset by lower revenue from the real estate group.

Sales and services contributed 72% of the total revenue in 2007 and 76% in 2006.

Equity in net earnings of associates and joint ventures – 18% increase from ₱8,253mln to ₱9,708mln

Largely due to higher equity earnings generated from the associates of the real estate and international groups and the parent company.

This account is 12% of the total revenue in 2006 and in 2007.

Interest income – 11% increase from ₱1,521mln to ₱1,693mln

Due to higher investible funds in 2007.

This account is 2% of the total revenue in 2007 and in 2006.

Other income – 53% increase from ₱6,998mln to ₱10,728mln

Largely due to capital gains from sale of shares and higher forex gains.

This account is 14% and 10% of the total revenue in 2007 and in 2006, respectively.

Cost of sales and services – 6% increase from ₱40,857mln to ₱43,169mln

Relative to higher sales.

Cost of sales and services is 74% and 76% of the total costs and expenses for the period ending 31 December 2007 and 2006, respectively.

General and administrative expenses – 23% increase from ₱7,708mln to ₱9,498mln

Largely due to the GAE of the new subsidiary, higher manpower costs, depreciation and amortization expenses of the electronics, information technology and business process outsourcing services group.

This account is 16% and 14% of the total costs and expenses for the period ending 31 December 2007 and 2006, respectively.

Interest expense and other financing charges – 18% decrease from ₱5,024mln to ₱4,120mln

Due to reduced average funding costs. As of 31 December 2007 this account is 7% of the total costs and expenses vs 9% in 31 December 2006.

Other charges – 306% increase from ₱387mln to ₱1,570mln

Due to impairment loss on goodwill of the electronics, information technology and business process outsourcing services group and extraordinary charges of the real estate group. As of 31 December 2007 this account is 3% of the total costs and expenses vs 1% in December 2006.

Provision for income tax – 5% increase from ₱1,877mln to ₱1,972mln

Due mainly to higher taxes paid by the parent company and the electronics, information technology and business process outsourcing services group.

## 2006

It was another record year for Ayala Corporation as net income reached an all-time high of ₱12.2 billion, 49% higher than 2005 net income of ₱8.2 billion. This was a result of the strong earnings of the operating units, lower interest expense, and gains from share sales. At the holding company level, equity earnings excluding dilution gains booked in 2005 grew by 12% to ₱12.3 billion as all key businesses posted significant earnings growth. Earnings were further enhanced by capital gains of ₱4.7 billion from the sale of shares in Ayala Land, BPI, and Globe. This monetization initiative is in line with the company's strategy to realize values from existing investments and reallocate resources into new high growth businesses as well as further reduce debt. Net debt at the holding company level by year-end was significantly lower at US\$462 million.

On a consolidated basis, sales and services rose by 54% to ₱53.4 billion. The substantial increase is attributed to Ayala Land's increased sales of land and condominium units during the year as demand remained brisk for residential projects across all market segments. Its revenues from its commercial center operations likewise contributed to the strong revenue growth as the year saw higher basic rent, the full operation of Phase 1B of Market! Market!, and higher occupancy rates. The electronics business also contributed to pushing consolidated revenues higher as IMI's revenues more than doubled during the year, reflecting the impact of the acquisition of Speedy Tech as well as organic growth. The auto dealerships likewise contributed to revenue growth with Ayala Auto's sales up 24% year-on-year.

Equity in net earnings of associates and joint ventures was relatively flat in 2006 at ₱8.3 billion as 2005 included dilution gains from the initial public offering of Manila Water in March 2005. This primarily reflects Ayala's share in the net earnings of BPI, Globe, and Manila Water. All three businesses posted record net income in 2006, with BPI's up 8% to ₱9.0 billion, Globe up 14% to ₱11.8 billion, and Manila Water's by 19% to ₱2.4 billion.

Interest fees, rental, investment and other income grew by 11% to ₱8.5 billion largely due to gains from the sale of shares of Ayala Land, BPI, and Globe. Ayala monetized some of these shares in view of new investments it is currently making in the business process outsourcing sector as well as an investment in a private equity real estate fund which has development projects lined up overseas. The sale of these shares allowed us to realize values from these long-time investments and also gave us the flexibility to pay out, for the first time in a decade, special cash dividends to shareholders.

Consolidated cost of sales and services increased by 56% to ₱40.9 billion and moved much in line with revenue growth. General and administrative expenses increased by 28% to ₱7.7 billion as a result of higher payroll costs due to additional hiring to support the expansion initiatives at IMI and Ayala Land. Consolidated interest and other charges declined by 28% to ₱5.4 billion. This was a result of a combination of lower debt at the parent level as well as Ayala Land's asset write-offs in 2005.

Consolidated cash and cash equivalents increased slightly to ₱23.1 billion as of year-end 2006 from ₱24.0 billion at the beginning of the year. The increase was mainly due to higher cash levels at the parent level given the strong cash dividend flows upstreamed by the operating units and various fund raising initiatives. Total cash dividends received from subsidiaries reached ₱5.5 billion.

By year-end 2006, net debt at the parent company level declined to US\$462 million from US\$563 million at the beginning of the year. A portion of our debt was paid in 2006 through the issuance of ₱5.8 billion in Series B preferred shares which now forms part of our stockholders' equity. While the preferred B shares do not have a fixed redemption period, Ayala has the option to redeem these shares after five years. This has caused the company's debt mix to move substantially in favor of the peso with 69% of the debt in local currency and 31% in US dollars. The current level of net debt puts the net debt-to-equity ratio down to 0.29 to 1 from 0.49 to 1 at the beginning of the year.

At the consolidated level, total debt also declined by 12% to ₱52.9 billion from ₱60.4 billion with consolidated net debt to equity at 0.39 to 1. Total stockholders' equity at year-end reached ₱77.1 billion up 26% from the previous year.

In the Philippine Stock Exchange, the company's stock price closed at a year-high of ₱590.00 per share, buoyed by the company's positive fundamentals and the market's generally robust performance. The strong peso, steady inflation, interest rates at all-time lows, sustained economic growth and well-contained budget deficit have all contributed to sustaining the market's bullish momentum. The generally upbeat mood throughout the year pushed the Philippine Composite Index (Phisix) to close 42% higher year-on-year at 2,982.54.

Ayala's listed operating units performed well. Ayala Land closed the year with a 54% increase in its share price to ₱15.25. BPI rose 40% to ₱63.50 at year-end. Globe advanced 68% to ₱1,235.00 and Manila Water gained 52% to close at ₱9.40.

Ayala Corporation's market capitalization at the end of the year reached ₱203.45 billion, the third highest among locally listed issues. Collectively, the market cap of the five listed Ayala companies accounted for 29% of the Phisix's total market capitalization. The 87% increase in Ayala's share price from its year-end 2005 level and the higher full-year dividend yield of around 2% resulted in an estimated total return to shareholders of 89% from end-2005.

**Causes for any material changes  
(Increase or decrease of 5% or more in the financial statements)**

Balance Sheet items  
(2006 Vs 2005)

Accounts and notes receivable – 54% increase from ₱11,308mln to ₱17,470mln

Largely due to receivables from the sale of shares, increased sales at new and existing projects and higher corporate withholding tax by the real estate group, advances by the international group to finance new investments and increased sales by the electronics, information technology and business process outsourcing services and automotive groups. As a percentage to total assets, accounts and notes receivable increased from 7% as of 31 December 2005 to 10% as of 31 December 2006.

Inventories – 9% increase from ₱8,999mln to ₱9,804mln

Attributable to the real estate group's construction accomplishment at residential building projects and continued development of residential subdivision projects. Inventories remained at 5% of the total assets as of 31 December 2006 and 31 December 2005.

Other current assets – 81% increase from ₱2,190mln to ₱3,961mln

Due to advances on land, increase in marketable securities and higher input VAT by the real estate group, inclusion of accounts of a new subsidiary under the electronics, information technology and business process outsourcing services group and additional investments in marketable securities by the international group. Other current assets increased to 2% of the total assets as of 31 December 2006 from 1% as of 31 December 2005.

Noncurrent assets held for sale – 100% increase to ₱3,658mln

Represents total assets of Makati Property Ventures Inc., a member of the real estate group and investment in Hermill Investment Pte. Ltd. of the international group classified as noncurrent assets held for sale.

Noncurrent account and notes receivable – 55% decrease from ₱5,631mln to ₱2,520mln

Mainly due to sale of receivables by one of the companies of the real estate group. As a percentage to total assets, noncurrent account and notes receivable slightly decreased from 3% as of 31 December 2005 to 1% as of 31 December 2006.

Investments in associates and joint ventures – 7% increase from ₱63,808mln to ₱68,569mln

Investments in associates joint ventures and others includes the Company's and its subsidiaries' investments in various affiliates which are being accounted for under the equity method. These affiliates are Bank of the Philippine Islands, Globe Telecom and Manila Water Corporation, among others.

The increase is largely due to the 2006 equity in earnings from affiliates and additional equity infusion by subsidiaries in an Asian private equity real estate fund and fund management company. This account is 38% of the total assets as of 31 December 2005 and 31 December 2006.

Investment in bonds and other securities – 67% increase from ₱2,073mln to ₱3,462mln

Primarily due to new investments made in 2006 by the electronics, information technology and business process outsourcing services group and revaluation of investments partly offset by the sale of securities at the Parent Company level. As a percentage to total assets, this account is 2% and 1% as of 31 December 2006 and 31 December 2005, respectively.

Property, plant and equipment – 9% decrease from ₱9,918mln to ₱9,057mln

Reclassification by the real estate group to Noncurrent assets held for sale partly offset by the inclusion of assets of the newly acquired subsidiaries under the electronics, information technology and business process outsourcing services group. This account is 6% and 5% of the total assets as of 31 December 2005 and 31 December 2006, respectively.

Pension assets – 14% decrease from ₱236mln to ₱203mln

Lower pension assets of the electronics, information technology and business process outsourcing services group. This account remained at 0.1% of the total assets as of 31 December 2006 and 31 December 2005.

Intangible Assets – 55% increase from ₱2,996mln to ₱4,631mln

Largely due to the acquisition of a new subsidiary partly offset by the amortization of intangible assets by the electronics, information technology and business process outsourcing services group. As a percentage to total assets, this account is 3% as of 31 December 2006 and 2% as of 31 December 2005.

Other noncurrent assets – 8% decrease from ₱1,947mln to ₱1,785mln

Due to liquidation of advances made by the real estate group to a landowner and lower deferred charges by the Parent Company. As a percentage to total assets, this account remained at 1% as of 31 December, 2005 and 31 December 2006.

Accounts payable and accrued expenses – 6% increase from ₱17,311mln to ₱18,326mln

Primarily due to higher payables to contractors and suppliers and higher VAT and expanded withholding tax payable by the real estate group, inclusion of payables of the newly acquired companies of the electronics, information technology and business process outsourcing services group and the Parent Company's higher dividends payable partly offset by lower interest payable due to lower loan balance. As of 31 December 2006 and 31 December 2005, this account is at 23% and 20% of the total liabilities, respectively.

Short-term debt – 59% decrease from ₱6,154mln to ₱2,504mln

Largely due to payment of short-term debt by the electronics, information technology and business process outsourcing services group used to finance acquisition of new companies in 2005. As of 31 December 2006 and 31 December 2005, this account is at 3% and 7% of the total liabilities, respectively.

Income-tax payable – 8% increase from ₱273mln to ₱296mln

Due to higher income subject to income tax.

Current portion of long-term debt – 214% increase from ₱2,985mln to ₱9,360mln

Reclassification of the real estate group's ₱3bln bonds which will mature in April 2007, as well as reclassification of the Parent Company's and the electronics, information technology and business process outsourcing services group's current maturing loans. As a percentage to total liabilities, current portion of long-term debt is 12% and 4% as of 31 December 2006 and 31 December 2005, respectively.

Cumulative redeemable preferred shares (current portion) – 100% decrease from ₱2,230mln

Redemption of the ₱2,230mln redeemable preferred shares in 2006 by the Parent Company. As a percentage to total liabilities, the cumulative redeemable preferred shares is 3% as of 31 December 2005.

Other current liabilities – 47% increase from ₱986mln to ₱1,453mln

Largely due to higher buyer deposits from various residential projects by the real estate group and revaluation of advances by the Parent Company. This is 2% and 1% of the total liabilities as of 31 December 2006 and 31 December 2005, respectively.

Liabilities Directly Associated with Noncurrent Assets Held for Sale– 100% increase to ₱469mln

Represents total liabilities of Makati Property Ventures Inc., a member of the real estate group classified as noncurrent assets held for sale.

Long-term debt – 17% decrease from ₱46,507mln to ₱38,518mln

Mainly due to payment of loans and reclassification to current portion. As a percentage to total liabilities, long-term debt is at 48% and 55% as of 31 December 2006 and 31 December 2005, respectively.

Deferred tax liabilities – 42% increase from ₱312mln to ₱444mln

Higher tax liability from prior years' installment sales of the real estate group due to shift in revenue recognition from percentage of collection to percentage of completion. As a percentage to total liabilities this account is 0.6% as of 31 December 2006 and 0.4% as of 31 December 2005.

Pension and other benefits – 12% increase from ₱434mln to ₱488mln

Mainly due to the Parent Company's increase in retirement fund contribution. As a percentage to total liabilities, pension and other benefits slightly increased from 0.5% as of 31 December 2005 to 0.6% as of 31 December 2006.

Other noncurrent liabilities – 14% increase from ₱5,370mln to ₱6,141mln

Higher retention payable and deferred interest income by the real estate group. As a percentage to total liabilities, this account is at 8% as of 31 December 2006 and 6% as of 31 December 2005.

Paid-up-Capital – 36% increase from ₱16,960mln to ₱23,138mln

Due mainly to the issuance of ₱5.8bln preferred shares in 2006

Share-based payments – 15% decrease from ₱656mln to ₱558mln

Mainly due to additional stock options exercised.

Cumulative translation adjustment – 151% decrease from ₱587mln to (₱298mln)

Mainly due to forex rate changes.

Net unrealized gain on available-for-sale investments 335% increase from ₱478mln to ₱2,079mln

Largely to increase in value of various investments of an affiliate bank and the electronics, information technology and business process outsourcing services group.

Minority interest – 14% increase from ₱21,590mln to ₱24,699mln

Largely due to share of minority holders in the 2006 net income and increased share due to sale of shares by the equity holders of Ayala Corporation.

Income Statement items

(YTD December 2006 Vs YTD December 2005)

Sales and services – 54% increase from ₱34,638mln to ₱53,394mln

Higher revenues from residential developments, shopping centers, office rentals and support businesses of the real estate group, contributions from the operations of newly acquired companies by the electronics, information technology and business process outsourcing services group and higher sales volume by the automotive group.

Sales and services contributed 76% and 69% of the total revenue in 2006 and in 2005, respectively.

Equity in net earnings of associates and joint ventures – 0.6% increase from ₱8,202mln to ₱8,253mln

Largely due to higher share in net earnings from various affiliates such as Bank of the Philippine Islands, Globe Telecom and Ayala Land Inc.'s affiliates such as Alabang Commercial Corporation and Cebu Holdings, Inc., partly offset by the absence of dilution gain arising from Manila Water Corporation's initial public offering in 2005.

In 2006, this account is 12% of the total revenue lower than the 16% in 2005.

Interest fees, rental investment and other income – 11% increase from ₱7,702mln to ₱8,519mln

Largely due to capital gains from sale of shares in 2006. This account is 12% of the total income in 2006, lower than the 15% in 2005.

Cost of sales and services – 56% increase from ₱26,170mln to ₱40,857mln

Relative to higher sales. This account is 76% of total costs and expenses in 2006 compared to 66% in 2005.

General and administrative expenses – 28% increase from ₱6,011mln to ₱7,708mln

Due to higher payroll and benefits costs and expansion of some subsidiaries. This amount is 14% of total costs and expenses in 2006, lower than the 15% in 2005.

Interest and other charges – 28% decrease from ₱7,563mln to ₱5,411mln

Due to provisions for decline in value of assets intended to be sold and write-off of deferred charges of the real estate group in 2005 and lower interest payables due to lower debt levels in 2006 at the parent company level. This account is 10% of total costs and expenses in 2006 and significantly lower than the 19% in 2005

Provision for income tax – 124% increase from ₱839mln to ₱1,877mln

Lower final tax rate in 2005 on capital gains in AIVI transaction coupled with higher corporate income tax rate in 2006.

## II. MARKET PRICE OF AND DIVIDENDS ON THE REGISTRANT'S COMMON EQUITY

### A) Principal Market where the registrant's Common equity is traded.

The following table shows the high and low prices (in PHP) of Ayala Corporation's shares in the Philippine Stock Exchange for the year 2006 and 2007:

	2007		2006 *	
	High	Low	High	Low
1 <sup>st</sup> qtr *	550.00	433.33	304.17	264.58
2 <sup>nd</sup> qtr	580.00	466.67*	393.75	279.17
3 <sup>rd</sup> qtr	585.00	402.50	397.92	308.33
4 <sup>th</sup> qtr	645.00	495.00	491.67	377.08

\* adjusted to reflect the 20% stock dividend declared in May 2007

The market capitalization of the Company as of end-2007, based on the closing price of ₱565.00/share, was approximately ₱234.12 billion.

The price information of Ayala Common Shares and Ayala Preferred "B" Shares as of the close of the latest practicable trading date, 26 February 2008, is ₱432.50 and ₱115.00, respectively.

### B) Holders

There are approximately 7,826 holders of common shares as of 31 January 2008. The following are the top 20 holders of the common shares of the Company:

	Stockholder Name	No. of Common Shares	Percentage (of Common Shares)
1.	Mermac, Inc.	210,895,275	50.96%
2.	PCD Nominee Corporation (Non-Filipino)	111,677,732	26.98%
3.	Mitsubishi Corporation	43,803,848	10.58%
4.	PCD Nominee Corporation (Filipino)	21,069,750	5.09%
5.	Shoemart, Inc.	13,356,674	3.23%
6.	Henry Sy, Sr.	1,080,530	0.26%
7.	ESOWN Administrator 2006	642,904	0.16%
8.	ESOWN Administrator 2007	619,912	0.15%
9.	Philippine Remnants Co., Inc.	571,560	0.14%
10.	ESOWN Administrator 2005	499,608	0.12%
11.	BPI TA 14105123 FAO Consuelo Zobel Alger Foundation	316,381	0.08%
12.	Cygnet Development Corporation	306,763	0.07%
13.	Sysmart Corporation	254,659	0.06%
14.	Mitsubishi Logistics Corporation	250,356	0.06%
15.	Antonio O. Olbes	195,993	0.05%
16.	Eduardo O. Olbes	163,328	0.04%
17.	Aristón Estrada, Jr.	161,040	0.04%
18.	AC ESOP/ESOWN Account	136,545	0.03%
19.	Andre Jon Tiu	109,442	0.03%
20.	Telengtán Brothers & Sons, Inc.	95,040	0.02%

As of 31 January 2008, 54.81% or 200,722,429 Common and 57,905,950 Preferred "B" shares are owned by the public.

C) *Dividends*

<b><i>Stock Dividends</i></b>		
PERCENT	RECORD DATE	PAYMENT DATE
20%	April 16, 2004	May 12, 2004
20%	May 22, 2007	June 18, 2007

There were no stock dividend declarations from 2005 to 2006.

<b><i>Cash Dividends – 2006</i></b>			
CLASS	PAYMENT DATE	RATE	TERM / RECORD DATE
<i>On common shares</i>	January 31, 2006	2.00/share	January 6, 2006
	July 28, 2006	6.00/share	July 6, 2006

<b><i>Cash Dividends – 2007</i></b>			
CLASS	PAYMENT DATE	RATE	TERM / RECORD DATE
<i>On common shares</i>	January 30, 2007	2.00/share	January 5, 2007
	July 31, 2007	4.00/share	July 6, 2007
	November 5, 2007	2.00/share	October 9, 2007
	January 29, 2008	2.00/share	January 4, 2008

*Dividend policy*

Dividends declared by the Company on its shares of stocks are payable in cash or in additional shares of stock. The payment of dividends in the future will depend upon the earnings, cash flow and financial condition of the Company and other factors.

D) *Recent Sale of Securities*

There were a total of 185,618 shares issued in 2007 representing exercise of stock options by the Company's executives. The aforesaid issuance of shares was covered by the Commission's approval of the Company's Stock Option Plan in December 2005.

E) *Corporate Governance*

- a. The evaluation system which was established to measure or determine the level of compliance of the Board of Directors and top level management with its Manual of Corporate Governance consists of a Board Performance Assessment which is accomplished by the Board of Directors indicating the compliance ratings. The above is submitted to the Compliance Officer who issues the required certificate of compliance with the Company's Corporate Governance Manual to the Securities and Exchange Commission.
- b. To ensure good governance, the Board establishes the vision, strategic objectives, key policies, and procedures for the management of the company, as well as the mechanism for monitoring and evaluating Management's performance. The Board also ensures the presence and adequacy of internal control mechanisms for good governance.
- c. There were no deviations from the Company's Manual of Corporate Governance. The Company has adopted in the Manual of Corporate Governance the leading practices and principles of good corporate governance, and full compliance therewith has been made since the adoption of the Manual.
- d. The Company is taking further steps to enhance adherence to principles and practices of good corporate governance.

**Upon the written request of the stockholders, the Corporation undertakes to furnish said stockholder with a copy of SEC Form 17-A free of charge. Any written request for a copy of SEC Form 17-A shall be addressed to the following:**

**Ayala Corporation  
34<sup>th</sup> Floor, Tower One and Exchange Plaza  
Ayala Triangle, Ayala Avenue  
Makati City**

**Attention: Mr. Rufino Luis T. Manotok  
Chief Finance Officer**

## **ANNEX “C”**

### **NATURE AND SCOPE OF BUSINESS**

Ayala Corporation is the holding company of one of the largest and most diversified business groups in the Philippines. It maintains a leading presence in real estate development (Ayala Land, Inc.), financial services (Bank of the Philippine Islands), telecommunications (Globe Telecom, Inc.), water delivery, sewerage and sanitation services (Manila Water Company, Inc.), electronics manufacturing service (Integrated Micro-electronics, Inc.), automotive dealerships (Ayala Automotive Holdings Corp.), technology-related investments (Azalea Technology Investments, Inc.), investments in business process outsourcing (LiveIt Solutions, Inc.), and overseas real estate investments (Ayala International Pte Ltd). The company was founded in 1834, incorporated in 1968, and was listed on the Philippine Stock Exchange (then Makati Stock Exchange) in 1976.

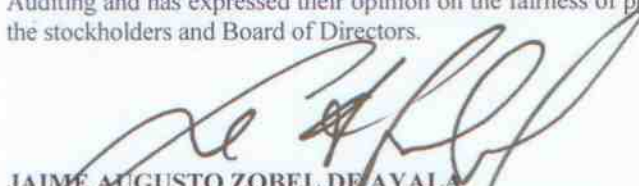
**STATEMENT OF MANAGEMENT'S RESPONSIBILITY  
FOR FINANCIAL STATEMENTS**

The management of Ayala Corporation is responsible for all information and representations contained in the consolidated balance sheets as at December 31, 2007 and 2006, and the consolidated statements of income, changes in equity and cash flows for each of the three years in the period ended December 31, 2007, and the summary of significant accounting policies and other explanatory notes. The consolidated financial statements have been prepared in accordance with Philippine Financial Reporting Standards and reflect amounts that are based on the best estimates and informed judgment of management with an appropriate consideration to materiality.

In this regard, management maintains a system of accounting and reporting which provides for the necessary internal controls to ensure that transactions are properly authorized and recorded, assets are safeguarded against unauthorized use or disposition and liabilities are recognized. The management likewise discloses to the Company's Audit Committee and to its external auditor: (i) all significant deficiencies in the design or operation of internal controls that could adversely affect its ability to record, process, and report financial data; (ii) material weaknesses in the internal controls, and (iii) any fraud that involves management or other employees who exercise significant roles in internal controls.

The Board of Directors reviews the consolidated financial statements before such statements are approved and submitted to the stockholders of the Company.

SyCip Gorres Velayo & Co., the independent auditors appointed by the Board of Directors and stockholders, has audited the consolidated financial statements of the Company and its Subsidiaries in accordance with Philippine Standards on Auditing and has expressed their opinion on the fairness of presentation upon completion of such audit, in their report to the stockholders and Board of Directors.



**JAIMÉ AUGUSTO ZOBEL DE AYALA**  
Chairman, Board of Directors and Chief Executive Officer



**FERNANDO ZOBEL DE AYALA**  
President and Chief Operating Officer

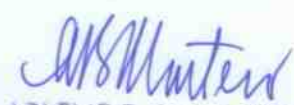


**RUFINO LUIS T. MANOTOK**  
Chief Finance Officer

SUBSCRIBED AND SWORN to before me this FEB 20 2008 at Makati City, affiants exhibiting to me their respective Community Tax Certificates, to wit:

<u>Name</u>	<u>CTC No.</u>	<u>Date &amp; Place of Issue</u>
Jaime Augusto Zobel de Ayala	19324091	15 February 2008 - Makati City
Fernando Zobel de Ayala	19324093	15 February 2008 - Makati City
Rufino Luis T. Manotok	24708186	30 January 2008 - Muntinlupa City

Doc. No. 98 ;  
Page No. 21 ;  
Book No. X1 ;  
Series of 2008.



**ARLENE B. MONIERO**  
Notary Public Until 31 Dec. 2008  
PTR No. 0987105J - 09 Jan. 2008  
Issued at Makati City  
TIN 178-486-374

AYALA CORPORATION AND SUBSIDIARIES

Consolidated Financial Statements  
December 31, 2007 and 2006  
and Years ended December 31, 2007, 2006 and 2005

and

Independent Auditors' Report



*Quality In Everything We Do*

## **INDEPENDENT AUDITORS' REPORT**

The Stockholders and the Board of Directors  
Ayala Corporation

We have audited the accompanying consolidated financial statements of Ayala Corporation and Subsidiaries, which comprise the consolidated balance sheets as at December 31, 2007 and 2006, and the consolidated statements of income, consolidated statements of changes in equity and consolidated statements of cash flows for each of the three years in the period ended December 31, 2007, and a summary of significant accounting policies and other explanatory notes. The financial statements of the Bank of the Philippine Islands and Subsidiaries, in which the Company has a 33.5% interest in 2007 and a 33.9% interest in 2006, were audited by other auditors whose report has been furnished to us, and our opinion on the consolidated financial statements, insofar as it relates to the amounts included for the Bank of the Philippine Islands and Subsidiaries, is based solely on the report of the other auditors. In the consolidated financial statements, the Company's investment in the Bank of the Philippine Islands and Subsidiaries is stated at ₱30,852 million and ₱29,860 million as of December 31, 2007 and 2006, respectively, and the Company's equity in the net income of the Bank of the Philippine Islands and Subsidiaries is stated at ₱3,291 million in 2007, ₱3,300 million in 2006 and ₱3,026 million in 2005.

### **Management's Responsibility for the Consolidated Financial Statements**

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with Philippine Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of consolidated 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 in the circumstances.

### **Auditors' Responsibility**

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Philippine 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 audit 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 and the report of other auditors are sufficient and appropriate to provide a basis for our audit opinion.

### **Opinion**

In our opinion, based on our audits and the report of the other auditors, the consolidated financial statements present fairly, in all material respects, the financial position of Ayala Corporation and Subsidiaries as of December 31, 2007 and 2006, and their financial performance and their cash flows for each of the three years in the period ended December 31, 2007 in accordance with Philippine Financial Reporting Standards.

SYCIP GORRES VELAYO & CO.

*Lucy L. Chan*

Lucy L. Chan

Partner

CPA Certificate No. 88118

SEC Accreditation No. 0114-AR-1

Tax Identification No. 152-884-511

PTR No. 0017583, January 3, 2008, Makati City

February 20, 2008



**AYALA CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
(Amounts in Thousands)

	December 31	
	2007	2006
<b>ASSETS</b>		
<b>Current Assets</b>		
Cash and cash equivalents (Notes 4 and 29)	₱36,835,549	₱20,391,301
Short-term investments (Notes 5 and 29)	3,687,606	2,927,928
Accounts and notes receivable - net (Notes 6, 28 and 29)	17,295,926	17,469,560
Inventories (Note 7)	8,842,535	9,391,896
Other current assets (Notes 8 and 29)	3,097,620	3,961,315
Total Current Assets	69,759,236	54,142,000
Noncurrent assets held for sale (Note 14)	–	3,658,484
	69,759,236	57,800,484
<b>Noncurrent Assets</b>		
Noncurrent accounts and notes receivable (Notes 6 and 29)	4,010,373	2,519,816
Land and improvements	16,200,601	16,587,010
Investments in associates and jointly controlled entities - net (Note 9)	71,560,257	68,568,683
Investment in bonds and other securities (Notes 10 and 29)	2,492,913	3,462,435
Investment properties - net (Note 11)	17,416,173	16,794,662
Property, plant and equipment - net (Notes 12 and 26)	8,492,845	9,057,075
Deferred tax assets - net (Note 22)	983,565	1,123,912
Pension assets (Note 24)	140,576	202,598
Intangible assets - net (Notes 13 and 21)	3,275,697	4,429,855
Other noncurrent assets	2,087,249	1,785,374
Total Noncurrent Assets	126,660,249	124,531,420
Total Assets	₱196,419,485	₱182,331,904
<b>LIABILITIES AND EQUITY</b>		
<b>Current Liabilities</b>		
Accounts payable and accrued expenses (Notes 15, 28 and 29)	₱22,261,167	₱18,325,716
Short-term debt (Notes 16 and 29)	2,634,148	2,504,007
Income tax payable	286,050	295,846
Current portion of long-term debt (Notes 16 and 29)	9,512,760	9,359,594
Other current liabilities	1,550,482	1,453,013
Total Current Liabilities	36,244,607	31,938,176
Liabilities directly associated with noncurrent assets held for sale (Note 14)	–	469,100
	36,244,607	32,407,276

(Forward)



	<b>December 31</b>	
	<b>2007</b>	<b>2006</b>
<b>Noncurrent Liabilities</b>		
Long-term debt - net of current portion (Notes 16 and 29)	<b>₱37,884,705</b>	₱38,517,839
Cumulative redeemable preferred shares (Notes 18 and 29)	–	2,500,000
Deferred tax liabilities - net (Note 22)	<b>155,756</b>	443,736
Pension liabilities (Note 24)	<b>531,552</b>	487,726
Other noncurrent liabilities (Note 17)	<b>6,817,643</b>	6,141,065
Total Noncurrent Liabilities	<b>45,389,656</b>	48,090,366
Total Liabilities	<b>81,634,263</b>	80,497,642
<b>Equity</b>		
Equity attributable to equity holders of Ayala Corporation		
Paid-up capital (Note 19)	<b>26,855,394</b>	23,137,948
Share-based payments (Note 25)	<b>603,949</b>	558,416
Cumulative translation adjustments (Note 19)	<b>(2,297,077)</b>	(298,310)
Retained earnings (Note 19)	<b>60,461,246</b>	51,659,261
Net unrealized gain on available-for-sale financial assets (Note 10)	<b>1,712,016</b>	2,078,522
Treasury stock (Note 19)	<b>(159,693)</b>	(310)
	<b>87,175,835</b>	77,135,527
Minority interests		
Minority interests - net of interest attributable to noncurrent assets held for sale	<b>27,609,387</b>	23,568,083
Minority interests attributable to noncurrent assets held for sale	–	1,130,652
	<b>27,609,387</b>	24,698,735
Total Equity	<b>114,785,222</b>	101,834,262
Total Liabilities and Equity	<b>₱196,419,485</b>	₱182,331,904

*See accompanying Notes to Consolidated Financial Statements.*



**AYALA CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF INCOME**  
(Amounts in Thousands, Except Earnings Per Share Figures)

	Years Ended December 31		
	2007	2006	2005
<b>REVENUE</b>			
Sales and services (Notes 11 and 28)	<b>₱56,578,214</b>	₱53,394,230	₱34,638,421
Equity in net income of associates and jointly controlled entities (Note 9)	<b>9,708,178</b>	8,252,898	8,202,301
Interest income	<b>1,693,045</b>	1,520,858	1,753,654
Other income (Note 20)	<b>10,728,375</b>	6,998,009	5,948,459
	<b>78,707,812</b>	70,165,995	50,542,835
<b>COSTS AND EXPENSES</b>			
Costs of sales and services (Notes 7, 11, 20 and 28)	<b>43,169,110</b>	40,857,337	26,170,055
General and administrative (Notes 20, 24, 25 and 28)	<b>9,498,306</b>	7,708,161	6,011,324
Interest expense and other financing charges (Notes 16 and 20)	<b>4,120,160</b>	5,024,052	5,343,433
Other charges (Note 20)	<b>1,569,944</b>	386,919	2,219,300
	<b>58,357,520</b>	53,976,469	39,744,112
<b>INCOME BEFORE INCOME TAX</b>	<b>20,350,292</b>	16,189,526	10,798,723
<b>PROVISION FOR INCOME TAX (Note 22)</b>			
Current	<b>1,979,820</b>	1,764,984	1,696,400
Deferred	<b>(7,825)</b>	112,175	(857,122)
	<b>1,971,995</b>	1,877,159	839,278
<b>INCOME BEFORE INCOME ASSOCIATED WITH NONCURRENT ASSETS HELD FOR SALE</b>	<b>18,378,297</b>	14,312,367	9,959,445
<b>INCOME ASSOCIATED WITH NONCURRENT ASSETS HELD FOR SALE - net of tax (Note 14)</b>	<b>624,788</b>	155,258	130,679
<b>NET INCOME</b>	<b>₱19,003,085</b>	₱14,467,625	₱10,090,124
Net Income Attributable to:			
Equity holders of Ayala Corporation	<b>₱16,197,557</b>	₱12,176,771	₱8,198,004
Minority interests	<b>2,805,528</b>	2,290,854	1,892,120
	<b>₱19,003,085</b>	₱14,467,625	₱10,090,124
<b>EARNINGS PER SHARE (Note 23)</b>			
Basic			
Income before income associated with noncurrent assets held for sale attributable to equity holders of Ayala Corporation	<b>₱36.63</b>	₱28.70	₱19.80
Net income attributable to equity holders of Ayala Corporation	<b>37.80</b>	28.82	19.90
Diluted			
Income before income associated with noncurrent assets held for sale attributable to equity holders of Ayala Corporation	<b>₱36.46</b>	₱28.56	₱19.72
Net income attributable to equity holders of Ayala Corporation	<b>37.62</b>	28.68	19.82

See accompanying Notes to Consolidated Financial Statements.



**AYALA CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY**  
**(Amounts in Thousands)**

	Paid-up Capital (Note 19)	Share-based Payments (Note 25)	Cumulative Translation Adjustments (Note 19)	Retained Earnings (Note 19)	Net Unrealized Gain on Available-for- Sale Financial Assets (Note 10)	Treasury Stock (Note 19)	Minority Interests	Total Equity
For the year ended December 31, 2007								
<b>At January 1, 2007</b>	₱23,137,948	₱558,416	(₱298,310)	₱51,659,261	₱2,078,522	(₱310)	₱24,698,735	₱101,834,262
Effect of adoption of Pre-need Rule 31, Pre-need Uniform Chart of Accounts by an associate (Note 9)	–	–	–	(85,010)	–	–	–	(85,010)
Adjustments to foreign currency translation	–	–	(1,998,767)	–	–	–	(358,643)	(2,357,410)
Changes in fair value of available-for- sale financial assets	–	–	–	–	(343,837)	–	34,900	(308,937)
Transferred to profit and loss	–	–	–	–	(22,669)	–	–	(22,669)
Net income recognized directly in equity	–	–	(1,998,767)	–	(366,506)	–	(323,743)	(2,689,016)
Net income for the year	–	–	–	16,197,557	–	–	2,805,528	19,003,085
Total income for the year	–	–	(1,998,767)	16,197,557	(366,506)	–	2,481,785	16,314,069
Issuance of shares	364,129	(154,441)	–	–	–	–	–	209,688
Additions to subscriptions receivable	(96,267)	–	–	–	–	–	–	(96,267)
Cost of share-based payments of Ayala Corporation	–	165,159	–	–	–	–	–	165,159
Cost of share-based payments of investees	–	34,815	–	–	–	–	201	35,016
Acquisition of treasury stocks	–	–	–	–	–	(159,383)	–	(159,383)
Cash dividends	–	–	–	(3,860,978)	–	–	–	(3,860,978)
Stock dividends	3,449,584	–	–	(3,449,584)	–	–	–	–
Increase in minority interests	–	–	–	–	–	–	962,291	962,291
Dividends paid to minority interests	–	–	–	–	–	–	(533,625)	(533,625)
<b>At December 31, 2007</b>	<b>₱26,855,394</b>	<b>₱603,949</b>	<b>(₱2,297,077)</b>	<b>₱60,461,246</b>	<b>₱1,712,016</b>	<b>(₱159,693)</b>	<b>₱27,609,387</b>	<b>₱114,785,222</b>



	<b>Paid-up Capital</b> (Note 19)	<b>Share-based Payments</b> (Note 25)	<b>Cumulative Translation Adjustments</b> (Note 19)	<b>Retained Earnings</b> (Note 19)	<b>Net Unrealized Gain on Available-for- Sale Financial Assets</b> (Note 10)	<b>Treasury Stock</b> (Note 19)	<b>Minority Interests</b>	<b>Total Equity</b>
For the year ended December 31, 2006								
At January 1, 2006	₱16,959,696	₱655,754	₱587,350	₱42,513,384	₱477,839	(₱310)	₱21,589,673	₱82,783,386
Adjustments to foreign currency translation	-	-	(885,660)	-	-	-	(146,104)	(1,031,764)
Changes in fair value of available-for-sale financial assets	-	-	-	-	2,487,563	-	(24,199)	2,463,364
Transferred to profit and loss	-	-	-	-	(886,880)	-	-	(886,880)
Net income recognized directly in equity	-	-	(885,660)	-	1,600,683	-	(170,303)	544,720
Net income for the year	-	-	-	12,176,771	-	-	2,290,854	14,467,625
Total income for the year	-	-	(885,660)	12,176,771	1,600,683	-	2,120,551	15,012,345
Issuance of shares	6,084,791	(227,101)	-	-	-	-	-	5,857,690
Collections of subscriptions receivable	93,461	-	-	-	-	-	-	93,461
Cost of share-based payments of Ayala Corporation	-	137,427	-	-	-	-	-	137,427
Cost of share-based payments of investees	-	(7,664)	-	-	-	-	-	(7,664)
Cash dividends	-	-	-	(3,030,894)	-	-	-	(3,030,894)
Increase in minority interests	-	-	-	-	-	-	1,879,066	1,879,066
Dividends paid to minority interests	-	-	-	-	-	-	(890,555)	(890,555)
At December 31, 2006	₱23,137,948	₱558,416	(₱298,310)	₱51,659,261	₱2,078,522	(₱310)	₱24,698,735	₱101,834,262



	Paid-up Capital (Note 19)	Share-based Payments (Note 25)	Cumulative Translation Adjustments (Note 19)	Retained Earnings (Note 19)	Net Unrealized Gain on Available-for- Sale Financial Assets (Note 10)	Treasury Stock (Note 19)	Minority Interests	Total Equity
For the year ended December 31, 2005								
At January 1, 2005	₱16,896,319	₱397,252	₱1,160,982	₱34,665,187	₱-	(₱102)	₱19,573,768	₱72,693,406
Effect of adoption of Philippine Accounting Standards No. 39	-	-	-	1,026,230	361,207	-	(59,054)	1,328,383
Adjustments to foreign currency translation	-	-	(573,632)	-	-	-	(67,674)	(641,306)
Changes in fair value of available-for- sale financial assets	-	-	-	-	138,684	-	28,740	167,424
Transferred to profit and loss	-	-	-	-	(22,052)	-	-	(22,052)
Net loss recognized directly in equity	-	-	(573,632)	-	116,632	-	(38,934)	(495,934)
Net income for the year	-	-	-	8,198,004	-	-	1,892,120	10,090,124
Total income for the year	-	-	(573,632)	8,198,004	116,632	-	1,853,186	9,594,190
Issuance of shares	95,815	(38,177)	-	-	-	-	-	57,638
Additions to subscriptions receivable	(32,438)	-	-	-	-	-	-	(32,438)
Cost of share-based payments of Ayala Corporation	-	142,950	-	-	-	-	-	142,950
Cost of share-based payments of investees	-	153,729	-	-	-	-	-	153,729
Acquisition of treasury stock	-	-	-	-	-	(208)	-	(208)
Cash dividends	-	-	-	(1,376,037)	-	-	-	(1,376,037)
Increase in minority interests	-	-	-	-	-	-	1,551,707	1,551,707
Dividends paid to minority interests	-	-	-	-	-	-	(1,329,934)	(1,329,934)
At December 31, 2005	₱16,959,696	₱655,754	₱587,350	₱42,513,384	₱477,839	(₱310)	₱21,589,673	₱82,783,386

See accompanying Notes to Consolidated Financial Statements.



**AYALA CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(Amounts in Thousands)**

	<b>Years Ended December 31</b>		
	<b>2007</b>	<b>2006</b>	<b>2005</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Income before income tax	<b>₱20,350,292</b>	₱16,189,526	₱10,798,723
Adjustments for:			
Interest and other financing charges - net of amount capitalized (Notes 16 and 20)	<b>4,120,160</b>	5,024,052	5,343,433
Depreciation and amortization (Note 20)	<b>2,988,879</b>	2,590,358	1,714,677
Cost of share-based payments (Note 25)	<b>288,050</b>	285,431	413,815
Impairment loss on goodwill (Note 20)	<b>662,591</b>	-	-
Equity in net income of associates and jointly controlled entities	<b>(9,708,178)</b>	(8,252,898)	(8,202,301)
Gain on sale of assets	<b>(8,844,822)</b>	(5,796,711)	(3,971,188)
Interest income	<b>(1,693,045)</b>	(1,520,858)	(1,753,654)
Other investment income	<b>(73,500)</b>	(285,227)	(596,676)
Operating income before changes in working capital	<b>8,090,427</b>	8,233,673	3,746,829
Decrease (increase) in:			
Accounts and notes receivable	<b>(2,254,055)</b>	(3,171,691)	(3,504,204)
Inventories	<b>1,981,833</b>	(251,543)	747,372
Other current assets	<b>863,696</b>	(1,777,903)	(581,725)
Increase (decrease) in:			
Accounts payable and accrued expenses	<b>4,318,671</b>	1,704,662	5,168,530
Other current liabilities	<b>97,469</b>	403,413	(346,614)
Net pension liabilities	<b>105,848</b>	89,130	(723,008)
Cash generated from operations	<b>13,203,889</b>	5,229,741	4,507,180
Interest received	<b>1,469,236</b>	1,510,885	1,797,536
Interest paid	<b>(3,837,504)</b>	(5,386,829)	(4,343,896)
Income taxes paid	<b>(1,989,616)</b>	(1,742,356)	(1,649,142)
Net cash provided by (used in) operating activities before cash items associated with noncurrent assets held for sale	<b>8,846,005</b>	(388,559)	311,678
Net cash provided by operating activities associated with noncurrent assets held for sale	-	291,672	241,186
Total cash provided by (used in) operating activities	<b>8,846,005</b>	(96,887)	552,864
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Proceeds from:			
Sale of investments	<b>15,152,209</b>	5,493,837	7,909,107
Disposals of property and equipment	<b>1,006,583</b>	313,755	527,540
Additions to:			
Short-term investments	<b>(759,678)</b>	(2,399,978)	(527,950)
Investments	<b>(6,258,142)</b>	(5,950,008)	(2,898,110)
Property, plant and equipment (Note 12)	<b>(4,368,019)</b>	(3,450,654)	(1,853,821)
Dividends received from associates and jointly controlled entities	<b>8,050,049</b>	4,248,500	4,499,186
(Forward)			



	<b>Years Ended December 31</b>		
	<b>2007</b>	2006	2005
Acquisitions through business combinations by a subsidiary - net of cash acquired (Note 21)	<b>(P326,030)</b>	(P1,641,092)	(P5,632,984)
Increase in other noncurrent assets	<b>(631,428)</b>	(10,076)	(661,629)
Cash balance of deconsolidated subsidiaries	-	(81)	-
Net cash provided by (used in) investing activities before cash items associated with noncurrent assets held for sale	<b>11,865,544</b>	(3,395,797)	1,361,339
Net cash provided by (used in) investing activities associated with noncurrent assets held for sale, including cash balance	<b>624,788</b>	(361,691)	2,071
Net cash provided by (used in) investing activities	<b>12,490,332</b>	(3,757,488)	1,363,410
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Proceeds from:			
Short-term and long-term debt	<b>21,742,528</b>	11,532,591	12,556,123
Issuance of common shares	<b>209,687</b>	57,690	-
Issuance of preferred shares	-	5,800,000	-
Proceeds from collections of (additions to) subscriptions receivable	<b>(96,267)</b>	93,461	(32,438)
Payments of short-term and long-term debt	<b>(24,827,895)</b>	(15,346,903)	(25,497,578)
Dividends paid	<b>(4,255,580)</b>	(3,781,584)	(2,423,750)
Redemption of preferred shares (Note 18)	<b>(2,500,000)</b>	(2,230,000)	(1,270,000)
Acquisition of treasury shares (Note 19)	<b>(159,383)</b>	-	-
Increase in:			
Other noncurrent liabilities	<b>676,578</b>	589,672	398,984
Minority interests in consolidated subsidiaries	<b>4,318,243</b>	4,234,992	3,171,745
Net cash provided by (used in) financing activities before cash items associated with noncurrent assets held for sale	<b>(4,892,089)</b>	949,919	(13,096,914)
Net cash used in financing activities associated with noncurrent assets held for sale	-	(187,120)	(271,572)
Net cash provided by (used in) financing activities	<b>(4,892,089)</b>	762,799	(13,368,486)
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>16,444,248</b>	(3,091,576)	(11,452,212)
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b> (Note 4)	<b>20,391,301</b>	23,482,877	34,935,089
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b> (Notes 4 and 29)	<b>P36,835,549</b>	P20,391,301	P23,482,877

See accompanying Notes to Consolidated Financial Statements.



# **AYALA CORPORATION AND SUBSIDIARIES**

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## **NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

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### **1. Corporate Information**

Ayala Corporation (the Company) is incorporated in the Republic of the Philippines. The Company's registered office and principal place of business is at Tower One, Ayala Triangle, Ayala Avenue, Makati City. The Company is a publicly listed company which is 50.90% owned by Mermac, Inc., 10.57% owned by Mitsubishi Corporation and the rest by the public.

The Company is the holding company of the Ayala Group (the Group), with principal business interests in real estate and hotels, financial services and bancassurance, telecommunications, electronics, information technology and business process outsourcing services, utilities, automotives, international and others.

The consolidated financial statements of Ayala Corporation and Subsidiaries as of December 31, 2007 and 2006 and for each of the three years in the period ended December 31, 2007 were endorsed for approval by the Audit Committee on February 14, 2008 and authorized for issue by the Executive Committee of the Board of Directors (BOD) on February 20, 2008.

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### **2. Summary of Significant Accounting Policies**

#### Basis of Preparation

The accompanying consolidated financial statements of the Group have been prepared on a historical cost basis, except for financial assets at fair value through profit or loss (FVPL), available-for-sale (AFS) financial assets and derivative financial instruments that have been measured at fair value. The consolidated financial statements are presented in Philippine Peso, and all values are rounded to the nearest thousand pesos (₱000) except when otherwise indicated.

#### Statement of Compliance

The consolidated financial statements of the Group have been prepared in compliance with Philippine Financial Reporting Standards (PFRS).

#### Basis of Consolidation

The consolidated financial statements comprise the financial statements of the Group as of December 31, 2007 and 2006 and for each of the three years in the period ended December 31, 2007. The financial statements of the subsidiaries are prepared for the same reporting year as the Company.

The consolidated financial statements are prepared using uniform accounting policies for like transactions and other events in similar circumstances. All significant intercompany transactions and balances, including intercompany profits and unrealized profits and losses, are eliminated in consolidation.

Subsidiaries are consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases.



The consolidated financial statements comprise the financial statements of the Company and the following wholly and majority-owned domestic and foreign subsidiaries:

	<b>Effective Percentages of Ownership</b>	
	<b>2007</b>	<b>2006</b>
<b>Real Estate and Hotels:</b>		
Ayala Land, Inc. (ALI) and subsidiaries	53.2*	57.8
Ayala Hotels, Inc. (AHI) and subsidiaries	76.6	78.9
<b>Electronics, Information Technology and Business Process Outsourcing Services:</b>		
Azalea Technology Investments, Inc. and subsidiaries (Azalea Technology)	100.0	100.0
Azalea International Venture Partners, Limited (AIVPL) (British Virgin Islands Company)	100.0	-
LiveIt Solutions, Inc. and subsidiaries (LiveIt)	100.0	100.0
HRMall, Inc.	100.0	100.0
Technopark Land, Inc.	78.8	78.8
Integrated Microelectronics, Inc. (IMI) and Subsidiaries**	67.9	70.4
<b>Automotive:</b>		
Ayala Automotive Holdings Corporation (AAHC) and subsidiaries	100.0	100.0
<b>International and Others:</b>		
Bestfull Holdings Limited (incorporated in Hong Kong) and subsidiaries (BHL Group)	100.0	-
Ayala International Pte. Ltd. (AIPL) (incorporated in Singapore) and subsidiaries	100.0	100.0
AC International Finance Limited (ACIFL) (Cayman Island Company) and subsidiary	100.0	100.0
AYC Finance Ltd. (British Virgin Islands Company)	100.0	100.0
Michigan Holdings, Inc. (MHI) and subsidiary	100.0	100.0
Ayala Aviation Corporation	100.0	100.0
Darong Agricultural and Development Corporation	100.0	100.0
PFC Properties, Inc. and subsidiary	99.9	99.9

\*The Company owns 75.25% of the total common and preferred shares of ALI.

\*\* a subsidiary of ACIFL through AYC Holdings, Ltd.

On November 29, 2007, the Company entered into a Deed of Assignment with AIVPL where the Company assigned its 250,000 shares in HRMall, Inc. (with original acquisition cost of ₱25.0 million representing 100% of HRMall's total outstanding stock) in exchange for 583,458 shares of AIVPL (with par value of US\$1.00 per share). This resulted in the Company having a direct ownership of 69% in AIVPL with Azalea Technology's ownership interest in AIVPL reduced to 31%.



Further, on December 19, 2007, the Company entered into a Subscription Agreement with Deed of Conversion of deposits for future subscriptions with AIVPL whereby the Company converted its deposits into equity by way of subscription to common shares of stock of AIVPL at an agreed Philippine Peso equivalent amounting to ₱407.8 million.

On June 20, 2007, AIPL and its subsidiaries (AIPL Group) have undergone restructuring wherein intermediate Hong Kong holding companies were formed such that BHL became the Company's holding company for the BHL Group which now includes the AIPL Group. BHL is a private limited company incorporated under Hong Kong laws.

On October 16, 2006, the Company entered into a Deed of Assignment with AYC Holdings, Ltd., a wholly owned subsidiary of ACIFL, where the Company assigned its 832,343,700 shares in IMI (with original acquisition cost of ₱520.6 million representing approximately 74.4% of IMI's total outstanding stock) in exchange for 104,112 shares of AYC Holdings (with par value of US\$100 per share). Further, the Company entered into a Deed of Assignment with ACIFL where the Company assigned its 104,112 shares in AYC Holdings, Ltd. (at a transfer value of US\$10.4 million) in exchange for 10,411,200 additional shares of ACIFL with a par value of US\$1 per share.

Acquisitions of subsidiaries are accounted for using the purchase method. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair value at the acquisition date, irrespective of the extent of any minority interests.

Any excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities is recognized as goodwill.

Any excess of the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities over the cost of business combination is recognized in the consolidated statement of income on the date of acquisition.

Minority interests represent the portion of profit or loss and net assets in subsidiaries not wholly owned and are presented separately in the consolidated statements of income and changes in equity and within the equity section in the consolidated balance sheets, separately from the Company's equity.

#### Changes in Accounting Policies

The accounting policies adopted are consistent with those of the previous financial year except as follows:

#### *Amendments to PFRSs and Philippine Interpretations effective in 2007*

The Group has adopted the following new and amended PFRS and Philippine Interpretations during the year.

- PFRS 7, *Financial Instruments: Disclosures*
- PAS 1 Amendment - *Presentation of Financial Statements*
- Philippine Interpretation IFRIC 10, *Interim Financial Reporting and Impairment*



The principal effects of these changes are as follows:

*PFRS 7, Financial Instruments: Disclosures*

PFRS 7 introduces new disclosures to improve the information about financial instruments. It requires the disclosure of qualitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk, including sensitivity analysis to market risk. It replaces disclosure requirements in PAS 32, *Financial Instruments: Disclosure and Presentation* and PAS 30, *Disclosure in the Financial Statements of Banks and Similar Financial Institutions*. It is applicable to all entities that report under PFRS.

The Group adopted the amendment to the transitional provisions of PFRS 7, as approved by the Financial Reporting Standards Council of the Philippines, which gives transitory relief with respect to the presentation of comparative information for the new risk disclosures about the nature and extent of risks arising from financial instruments. Accordingly, the Group does not need to present comparative information for the disclosures required by paragraphs 31- 42 of PFRS 7, unless the disclosure was previously required under PAS 32. Adoption of PFRS 7 resulted in additional disclosures, which are included throughout the consolidated financial statements. These disclosures include presenting the different classes of loans and receivables (see Note 6), rollforward of allowance for doubtful accounts (see Note 6), credit quality of financial assets (see Note 29), aging of past due but not impaired financial assets (see Note 29), and sensitivity analysis as to changes in interest and foreign exchange rates (see Note 29).

*PAS 1 Amendment - Presentation of Financial Statements*

The amendment to PAS 1 introduces disclosures about the level of an entity's capital and how it manages capital. The new disclosures are shown in Note 19 to the consolidated financial statements.

*Philippine Interpretation IFRIC 10, Interim Financial Reporting and Impairment (effective for annual periods beginning on or after November 1, 2006)*

The Group adopted the Interpretation beginning January 1, 2007, which prohibits the reversal of impairment losses on goodwill and AFS equity investments recognized in the interim financial reports even if impairment is no longer present at the annual balance sheet date. Adoption of the Interpretation did not have any significant impact on the consolidated financial statements.

Future Changes in Accounting Policies

The Group has not applied the following new and amended PFRS and Philippine Interpretations which are not yet effective for the year ended December 31, 2007:

*PFRS 8, Operating Segments (effective for annual periods beginning on or after January 1, 2009).*

PFRS 8 requires a management approach to reporting segment information. PFRS 8 will replace PAS 14, *Segment Reporting*, and is required to be adopted only by entities whose debt or equity instruments are publicly traded, or are in the process of filing with the Securities and Exchange Commission (SEC) for purposes of issuing any class of instruments in a public market. The Group will apply PFRS 8 in 2009 and will assess the impact of this Standard on its current manner of reporting segment information.



PAS 1, *Presentation of Financial Statements (Revised)* (effective for annual periods beginning on or after January 1, 2009)

The revised Standard requires that the statement of changes in equity includes only transactions with owners and all non-owner changes are presented in equity as a single line with details included in a separate statement. Owners are defined as holders of instruments classified as equity.

In addition, the amendment to PAS 1 provides for the introduction of a new statement of comprehensive income that combines all items of income and expense recognized in the statements of income together with 'other comprehensive income'. The revisions specify what is included in other comprehensive income, such as gains and losses on available-for-sale assets, actuarial gains and losses on defined benefit pension plans and changes in the asset revaluation reserve. Entities can choose to present all items in one statement, or to present two linked statements, a separate statement of income and a statement of comprehensive income. The Group will assess the impact of the Standard on its current manner of reporting all items of income and expenses.

PAS 23 Amendment - *Borrowing Costs* (effective for annual periods beginning on or after January 1, 2009)

The Standard has been amended to require capitalization of borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset. A qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale. In accordance with the transitional requirements in the amendment, this change in accounting for borrowing costs shall be accounted for prospectively. Accordingly, borrowing costs will be capitalized on qualifying assets with a commencement date after January 1, 2009. No changes will be made for borrowing costs incurred to this date that have been expensed. The Group does not expect that the adoption of this Standard will have a significant impact on the consolidated financial statements.

Philippine Interpretation IFRIC 11, *PFRS 2, Group and Treasury Share Transactions* (effective for annual periods beginning on or after March 1, 2007).

This Interpretation requires arrangements whereby an employee is granted rights to an entity's equity instruments to be accounted for as an equity-settled scheme by the entity even if the entity chooses or is required to buy those equity instruments (e.g., treasury shares) from another party, or the shareholder(s) of the entity provide the equity instruments needed. It also provides guidance on how subsidiaries, in their separate financial statements, account for such schemes when their employees receive rights to the equity instruments of the parent. The Group does not expect this Interpretation to have a significant impact on the consolidated financial statements.

Philippine Interpretation IFRIC 12, *Service Concession Arrangements* (effective for annual periods beginning on or after January 1, 2008).

This Interpretation establishes the accounting to be applied for certain infrastructures that is constructed, acquired or provided by the grantor for the purposes of meeting the concession.



IFRIC 12 prescribed the accounting for the rights which the Operator receives from the Grantor using either:

- Financial asset model wherein the Operator shall recognize a financial asset to the extent that it has an unconditional contractual right to receive cash from the Grantor. The Operator has an unconditional right to receive cash if the Grantor contractually guarantees to pay the Operator;
- Intangible asset model wherein the Operator shall recognize an intangible asset to the extent that it receives a right to charge the users (not an unconditional right to receive cash because the amounts are contingent on the extent that the public uses the service);
- Mixed model if the Operator is paid by the users, but the Grantor guarantees a certain minimum amount to be paid to the Operator, the Financial Asset Model is used to the extent of such amount.

This Interpretation becomes applicable for financial years beginning on or after January 1, 2008.

Based on Manila Water Company Inc.'s (MWCI) preliminary assessment, its service concession agreement with the Metropolitan Waterworks and Sewerage System (MWSS) would qualify under the Intangible asset model. The adoption of the Interpretation will require MWCI to recognize the fair value of its right to charge its customers which will result in an increase in asset and corresponding increase in liabilities. The present value of total estimated concession fee payments determined at inception and subsequent infrastructure expenditures will form part of the intangible assets. MWCI will use the straight-line method in amortizing its intangible assets.

Liabilities on concession agreement represent the present value of future payments to MWSS to cover the latter's payments of loans availed to fund the construction of such assets. The Concessionaire's obligation to pay arises as the debt is amortized by MWSS. Thus, concession assets and related liabilities refer to the present value at inception of concession agreement of future debt amortizations. The increase in intangible assets will give rise to a possible increase in amortization expense.

Based on MWCI's preliminary assessment, the adoption of IFRIC 12 on January 1, 2008 will result in an increase in the total assets and total liabilities by ₱2.9 billion and ₱3.5 billion respectively, and a decrease in the retained earnings as of January 1, 2008 by ₱0.6 billion (net of tax effect of ₱0.3 billion). The estimated impact on the Company is a decrease in the retained earnings balance as of January 1, 2008 by ₱0.2 billion.

Philippine Interpretation IFRIC 13, *Customer Loyalty Programmes (effective for annual periods beginning on or after July 1, 2008)*.

This Interpretation requires customer loyalty award credits to be accounted for as a separate component of the sales transaction in which they are granted and therefore part of the fair value of the consideration received is allocated to the awards credits and deferred over the period that the award credits are fulfilled. The Group does not expect this Interpretation to have a significant impact on the consolidated financial statements as no such scheme currently exists.



Philippine Interpretation IFRIC 14, *PAS 19 - Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction (effective for annual periods beginning on or after January 1, 2008)*.

This Interpretation provides guidance on how to assess the limit on the amount of surplus in a defined benefit scheme that can be recognized as an asset under PAS 19, *Employee Benefits*. It also explains how the pension asset or liability may be affected by a statutory or contractual minimum funding requirement. The Group does not expect this Interpretation to have a significant impact on the consolidated financial statements.

#### Cash and Cash Equivalents

Cash includes cash on hand and in banks. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash with original maturities of three months or less from dates of acquisition and which are subject to an insignificant risk of changes in value.

#### Financial Instruments

##### *Date of recognition*

The Group recognizes a financial asset or a financial liability in the consolidated balance sheet when it becomes a party to the contractual provisions of the instrument. Purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace are recognized on the settlement date.

##### *Initial recognition of financial instruments*

All financial assets and financial liabilities are recognized initially at fair value. Except for securities at FVPL, the initial measurement of financial assets includes transaction costs. The Group classifies its financial assets in the following categories: financial assets at FVPL, loans and receivables, held-to-maturity (HTM) investments, and AFS financial assets. The Group also classifies its financial liabilities into FVPL and other liabilities. The classification depends on the purpose for which the investments were acquired and whether they are quoted in an active market. The Group determines the classification of its financial assets at initial recognition and, where allowed and appropriate, re-evaluates such designation at every reporting date.

Financial instruments are classified as liabilities or equity in accordance with the substance of the contractual arrangement. Interest, dividends, gains and losses relating to a financial instrument or a component that is a financial liability, are reported as expense or income. Distributions to holders of financial instruments classified as equity are charged directly to stockholders' equity net of any related income tax benefits.

##### *Determination of fair value*

The fair value for financial instruments traded in active markets at the balance sheet date is based on their quoted market price or dealer price quotations (bid price for long positions and ask price for short positions), without any deduction for transaction costs. When current bid and asking prices are not available, the price of the most recent transaction provides evidence of the current fair value as long as there has not been a significant change in economic circumstances since the time of the transaction.



For all other financial instruments not listed in an active market, the fair value is determined by using appropriate valuation methodologies. Valuation methodologies include net present value techniques, comparison to similar instruments for which market observable prices exist, options pricing models, and other relevant valuation models.

*Day 1 profit*

Where the transaction price in a non-active market is different to the fair value from other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable market, the Group recognizes the difference between the transaction price and fair value (a Day 1 profit) in the consolidated statement of income under “Interest income” or “Interest expense and other financing charges” accounts unless it qualifies for recognition as some other type of asset. In cases where use is made of data which is not observable, the difference between the transaction price and model value is only recognized in the consolidated statement of income when the inputs become observable or when the instrument is derecognized. For each transaction, the Group determines the appropriate method of recognizing the ‘Day 1’ profit amount.

*Financial assets at FVPL*

Financial assets at FVPL include financial assets held for trading and financial assets designated upon initial recognition as at FVPL.

Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term. Derivatives, including separated embedded derivatives, are also classified as held for trading unless they are designated as effective hedging instruments or a financial guarantee contract. Gains or losses on investments held for trading are recognized in the consolidated statement of income under “Other income” or “Other charges” account. Interest earned or incurred is recorded in “Interest income” or “Interest expense and other financing charges” account while dividend income is recorded when the right of payments has been established.

Where a contract contains one or more embedded derivatives, the hybrid contract may be designated as financial asset at FVPL, except where the embedded derivative does not significantly modify the cash flows or it is clear that separation of the embedded derivative is prohibited.

Financial assets may be designated at initial recognition as at FVPL if the following criteria are met: (i) the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or recognizing gains or losses on them on a different basis; or (ii) the assets are part of a group of financial assets which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management strategy; or (iii) the financial instrument contains an embedded derivative that would need to be separately recorded.

The Group’s financial assets at FVPL pertain to government securities and other investment securities and derivatives not designated as hedges.



### Derivative Financial Instruments

The Group uses derivative financial instruments to hedge its risks associated with interest rate and foreign currency fluctuations. These derivative instruments provide economic hedges under the Group's policies but are not designated as accounting hedges. Any gains or losses arising from changes in fair value on derivatives that do not qualify for hedge accounting are taken directly to net profit or loss for the year under "Interest income", "Interest expense and other financing charges" or "Other income" account. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

The fair value of forward currency contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles. The fair value of interest rate swap contracts is determined by reference to market values for similar instruments.

An embedded derivative is separated from the host contract and accounted for as a derivative if all of the following conditions are met: a) the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract; b) a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and c) the hybrid or combined instrument is not recognized at fair value through profit or loss.

The Group's derivative assets pertain to nondeliverable currency forward contracts and structured currency options included under "Other current assets" account in the consolidated balance sheet.

### *HTM investments*

HTM investments are quoted nonderivative financial assets with fixed or determinable payments and fixed maturities that the Group has the positive intention and ability to hold to maturity. Where the Group sell other than an insignificant amount of HTM investments, the entire category would be tainted and reclassified as AFS investments. After initial measurement, these investments are measured at amortized cost using the effective interest rate method, less impairment in value. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the effective interest rate. The amortization is included in "Interest income" in the consolidated statements of income. Gains and losses are recognized in the consolidated statement of income when the HTM investments are derecognized or impaired, as well as through the amortization process. The losses arising from impairment of such investments shall be recognized in the consolidated statement of income under "Other charges" account.

The Group's HTM investments pertain to bonds included under the "Investments in bonds and other securities" account in the consolidated balance sheet.

### *Loans and receivables*

Loans and receivables are nonderivative financial assets with fixed or determinable payments that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale and are not designated as AFS or financial asset at FVPL. This accounting policy relates both to the balance sheet captions "Short-term investments" which arise primarily from unquoted debt securities, and "Accounts and notes receivable" (except for Advances to contractors).



After initial measurement, loans and receivables are subsequently measured at amortized cost using the effective interest rate method, less any allowance for impairment losses. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the effective interest rate. The amortization is included in the "Interest income" account in the consolidated statement of income. The losses arising from impairment of such loans and receivables are recognized under "Provision for doubtful accounts" account in the consolidated statement of income.

The Group's loans and receivables are included under the "Accounts and notes receivable" account in the consolidated balance sheet. Loans and receivables are included in current assets if maturity is within 12 months from the balance sheet date.

#### *AFS financial assets*

AFS investments are those which are designated as such or do not qualify to be classified as designated as FVPL, HTM, or loans and receivables.

Financial assets may be designated at initial recognition as AFS if they are purchased and held indefinitely, and may be sold in response to liquidity requirements or changes in market conditions. AFS investments include equity investments.

After initial measurement, AFS financial assets are measured at fair value. The unrealized gains or losses arising from the fair valuation of AFS financial assets are excluded from reported earnings and are reported as "Net unrealized gain on available-for-sale financial assets" (net of tax where applicable) in the consolidated statement of changes in equity.

When the security is disposed of, the cumulative gain or loss previously recognized in equity is recognized in the consolidated statement of income under the "Other income" or "Other charges" account. Where the Group holds more than one investment in the same security these are deemed to be disposed of on a first-in first-out basis. Interest earned on the AFS financial assets is reported as interest income using the effective interest rate. Dividends earned are recognized under "Other income" account in the consolidated statement of income when the right to receive payment is established. The losses arising from impairment of such investments are recognized under "Other charges" account in the consolidated statement of income.

When the fair value of AFS financial assets cannot be measured reliably because of lack of reliable estimates of future cash flows and discount rates necessary to calculate the fair value of unquoted equity instruments, these investments are carried at cost, less any allowance for impairment losses.

The Group's AFS financial assets pertain to investments in quoted and unquoted equity securities included under the "Investment in bonds and other securities" account in the consolidated balance sheet. AFS financial assets are included in current assets if expected to be realized within 12 months from balance sheet date.

#### Other Financial Liabilities

Other financial liabilities include short-term and long-term debts. All loans and borrowings are initially recognized at cost, being the fair value of the consideration received less directly attributable transaction costs.



After initial recognition, short-term and long-term debts are subsequently measured at amortized cost using the effective interest method. Amortized cost is calculated by taking into account any issue costs, and any discount or premium on settlement.

Gains and losses are recognized in the consolidated statement of income when the liabilities are derecognized or impaired, as well as through the amortization process.

#### Deposits and Retention Payable

Deposits and retention payable are initially measured at fair value. After initial recognition, deposits and retention payable are subsequently measured at amortized cost using effective interest rate method.

For deposits, the difference between the cash received and its fair value is deferred (included in the “Deferred credits” in the consolidated balance sheet) and amortized using the straight-line method under the “Sales and services” account in the consolidated statement of income.

#### Derecognition of Financial Assets and Liabilities

##### *Financial Asset*

A financial asset (or, where applicable a part of a financial asset or part of a group of financial assets) is derecognized where:

- the rights to receive cash flows from the assets have expired;
- the Group retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third-party under a “pass-through” arrangement; or
- the Group has transferred its right to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained the risks and rewards of the asset but has transferred control of the asset.

Where the Group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognized to the extent of the Group’s continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

##### *Financial Liability*

A financial liability is derecognized when the obligation under the liability is discharged or cancelled or has expired. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognized in the consolidated statement of income.



### Impairment of Financial Assets

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred ‘loss event’) and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganization and where observable data indicate that there is measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

#### *Loans and receivables and HTM investments*

For loans and receivables and HTM investments carried at amortized cost, the Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses for impairment. Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors’ ability to pay all amounts due according to the contractual terms of the assets being evaluated. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognized are not included in a collective assessment for impairment.

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset’s carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset’s original effective interest rate (i.e., the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced through use of an allowance account and the amount of the loss is charged to the consolidated statement of income under “Provision for doubtful accounts”. Interest income continues to be recognized based on the original effective interest rate of the asset. Loans, together with the associated allowance accounts, are written off when there is no realistic prospect of future recovery and all collateral has been realized. If, in a subsequent period, the amount of the estimated impairment loss decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed. Any subsequent reversal of an impairment loss is recognized in profit or loss, to the extent that the carrying value of the asset does not exceed its amortized cost at the reversal date.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of such credit risk characteristics as industry, past-due status and term.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. The methodology and assumptions used for estimating future



cash flows are reviewed

regularly by the Group to reduce any differences between loss estimates and actual loss experience.

*Assets carried at cost*

If there is an objective evidence that an impairment loss has been incurred on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, or on derivative asset that is linked to and must be settled by delivery of such an unquoted equity instrument, the amount of the loss is measured as the difference between the carrying amount and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset.

*AFS financial assets*

In case of equity investments classified as AFS financial assets, impairment would include a significant or prolonged decline in the fair value of the investments below its cost. Where there is evidence of impairment loss, the cumulative loss - measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognized in the consolidated statement of income - is removed from equity and recognized in the consolidated statement of income under "Other charges" account. Impairment losses on equity investments are not reversed through the consolidated statement of income. Increases in fair value after impairment are recognized directly in the consolidated statement of changes in equity.

In the case of debt instruments classified as AFS, impairment is assessed based on the same criteria as financial assets carried at amortized cost. Interest continues to be accrued at the original effective interest rate on the reduced carrying amount of the asset and is recorded as part of "Interest income" account in the consolidated statement of income. If, in subsequent year, the fair value of a debt instrument increased and the increase can be objectively related to an event occurring after the impairment loss was recognized in the consolidated statement of income, the impairment loss is reversed through the consolidated statement of income.

Offsetting Financial Instruments

Financial assets and financial liabilities are offset and the net amount reported in the consolidated balance sheet if, and only if, there is a currently enforceable legal right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the asset and settle the liability simultaneously. This is not generally the case with master netting agreements, and the related assets and liabilities are presented gross in the consolidated balance sheet.

Cumulative Redeemable Preferred Shares

Cumulative redeemable preferred shares that exhibit characteristics of a liability is recognized as a liability in the consolidated balance sheet. The corresponding dividends on those shares are charged as interest expense in the consolidated statement of income. Upon issuance, cumulative redeemable preferred shares are carried as a long-term liability on the amortized cost basis until extinguished on redemption.



### Inventories

Inventories are carried at the lower of cost and net realizable value (NRV). Costs incurred in bringing each product to its present location and condition are generally accounted for as follows:

Real estate inventories - cost includes those costs incurred for the development and improvement of properties, including capitalized borrowing costs.

Vehicles - purchase cost on specific identification basis.

Finished goods and work-in-process - determined on a moving average basis; cost includes direct materials and labor and a proportion of manufacturing overhead costs based on normal operating capacity.

Parts and accessories, materials, supplies and others - purchase cost on a moving average basis.

NRV for real estate inventories, vehicles, finished goods and work-in-process and parts and accessories is the estimated selling price in the ordinary course of business, less estimated costs of completion and estimated costs necessary to make the sale, while NRV for materials, supplies and others represents the related replacement costs.

### Noncurrent Assets Held for Sale

Noncurrent assets held for sale are carried at the lower of its carrying amount and fair value less costs to sell. At balance sheet date, the Group classifies assets as held for sale (disposal group) when their carrying amount will be recovered principally through a sale transaction rather than through continuing use. For this to be the case the asset must be available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets and its sale must be highly probable. For the sale to be highly probable, the appropriate level of management must be committed to a plan to sell the asset and an active program to locate a buyer and complete the plan must have been initiated. Further, the asset must be actively marketed for sale at a price that is reasonable in relation to its current fair value. In addition, the sale should be expected to qualify for recognition as a completed sale within one year from the date of classification.

The related results of operations and cash flows of the disposal group that qualified as discontinued operation are separated from the results of those that would be recovered principally through continuing use, and prior years' consolidated statement of income and cash flows are re-presented. Results of operations and cash flows of the disposal group that qualified as discontinued operation are presented in the consolidated statement of income and consolidated statement of cash flows as items associated with noncurrent assets held for sale.

### Land and Improvements

Land and improvements consist of properties for future development and are carried at the lower of cost or NRV. NRV is the estimated selling price in the ordinary course of business, less estimated cost of completion and estimated costs necessary to make the sale. Cost includes cost of purchase and those costs incurred for improvement of the properties.



### Investments in Associates and Jointly Controlled Entities

Investments in associates and jointly controlled entities are accounted for under the equity method. An associate is an entity in which the Group has significant influence and which is neither a subsidiary nor a joint venture. A joint venture is a contractual arrangement whereby two or more parties undertake an economic activity that is subject to joint control, and a jointly controlled entity is a joint venture that involves the establishment of a separate entity in which each venturer has an interest.

An investment in an associate is accounted for using the equity method from the date on which it becomes an associate. On acquisition of the investment, any difference between the cost of the investment and the investor's share of the net fair value of the associate's identifiable assets, liabilities and contingent liabilities is accounted for as goodwill or negative goodwill.

Under the equity method, investments in associates and jointly controlled entities are carried in the consolidated balance sheet at cost plus post-acquisition changes in the Group's share in the net assets of the investees, less any impairment in value. Goodwill relating to an associate is included in the carrying amount of the investment and is not amortized. The Group's share in the investee's post-acquisition profits or losses is recognized in the consolidated statement of income, and its share of post-acquisition movements in the investee's equity reserves is recognized directly in equity. Unrealized gains arising from intercompany transactions are eliminated to the extent of the Group's interest thereon. Unrealized losses are eliminated similarly but only to the extent that there is no evidence of impairment of the asset transferred. Dividends received are treated as a reduction of the carrying value of the investments.

The Group discontinues applying the equity method when their investments in investee companies are reduced to zero. Accordingly, additional losses are not recognized unless the Group has guaranteed certain obligations of the investee companies. When the investee companies subsequently reports profits, the Group resumes recognizing its share of the profits only after its share of the profits equals the share of net losses not recognized during the period the equity method was suspended.

The reporting dates of the investee companies and the Group are identical and the investee companies' accounting policies conform to those used by the Group for like transactions and events in similar circumstances.

### Investment Properties

Investment properties consist of properties that are held to earn rentals, and are not occupied by the companies in the Group. Investment properties, except for land, are carried at cost less accumulated depreciation and amortization and any impairment in value. Land is carried at cost less any impairment in value. Depreciation and amortization are computed using the straight-line method over the estimated useful lives of the assets, regardless of utilization. The estimated useful lives of investment properties are as follows:

Land improvements	5 years
Buildings	20-40 years



Investment properties are derecognized when either they have been disposed of or when the investment property is permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gains or losses on the retirement or disposal of an investment property are recognized in the consolidated statement of income in the year of retirement or disposal.

Transfers are made to investment property when there is a change in use, evidenced by ending of owner-occupation, commencement of an operating lease to another party or ending of construction or development. Transfers are made from investment property when, and only when, there is a change in use, evidenced by commencement of owner-occupation or commencement of development with a view to sale. Transfers between investment property, owner-occupied property and inventories do not change the carrying amount of the property transferred and they do not change the cost of the property for measurement or for disclosure purposes.

#### Property, Plant and Equipment

Property, plant and equipment, except for land, are carried at cost less accumulated depreciation and amortization and any impairment in value. Land is carried at cost less any impairment in value. The initial cost of property, plant and equipment consists of its construction cost or purchase price and any directly attributable costs of bringing the property, plant and equipment to its working condition and location for its intended use.

Construction-in-progress is stated at cost. This includes cost of construction and other direct costs. Construction-in-progress is not depreciated until such time that the relevant assets are completed and put into operational use.

Major repairs are capitalized as part of property, plant and equipment only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the items can be measured reliably. All other repairs and maintenance are charged against current operations as incurred.

Depreciation and amortization of property, plant and equipment commences once the property, plant and equipment are available for use and computed using the straight-line basis over the estimated useful life of the property, plant and equipment as follows:

Buildings and improvements	3-40 years
Machinery and equipment	3-10 years
Furniture, fixtures and equipment	2-10 years
Transportation equipment	3-5 years

Hotel property and equipment includes the following types of assets and their corresponding estimated useful lives:

Hotel buildings and improvements	30-50 years
Land improvements	30 years
Leasehold improvements	5-20 years
Furniture, furnishing and equipment	5 years
Machinery and equipment	5 years
Transportation equipment	5 years



The assets residual values, useful life and depreciation and amortization methods are reviewed periodically to ensure that the amounts, period and methods of depreciation and amortization are consistent with the expected pattern of economic benefits from items of property, plant and equipment.

When property, plant and equipment are retired or otherwise disposed of, the cost and the related accumulated depreciation and amortization and accumulated provision for impairment losses, if any, are removed from the accounts and any resulting gain or loss is credited or charged against current operations.

#### Intangible Assets

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is the fair value as at the date of acquisition. Subsequently, intangible assets are measured at cost less accumulated amortization and provision for impairment loss, if any. The useful lives of intangible assets with finite life are assessed at the individual asset level. Intangible assets with finite life are amortized over their useful life. Periods and method of amortization for intangible assets with finite useful lives are reviewed annually or earlier when an indicator of impairment exists.

The estimated useful life of intangible assets follows:

Customer relationships	2-5 years
Order backlog	6 months
Unpatented technology	5 years
Developed software	2 years
Licenses	3 years

A gain or loss arising from derecognition of an intangible asset is measured as the difference between the net disposal proceeds and the carrying amount of the intangible asset and is recognized in the consolidated statement of income when the intangible asset is derecognized.

#### Impairment of Non-financial Assets

The Group assesses as at reporting date whether there is an indication that an asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Group makes an estimate of the asset's recoverable amount. An asset's recoverable amount is calculated as the higher of the asset's or cash-generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessment of the time value of money and the risks specific to the asset. Impairment losses of continuing operations are recognized in the consolidated statement of income in those expense categories consistent with the function of the impaired asset.



For assets excluding goodwill, an assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. If that is the case, the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation and amortization, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in the consolidated statement of income unless the asset is carried at revalued amount, in which case the reversal is treated as revaluation increase. After such a reversal, the depreciation charge is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

*Investments in associates and jointly controlled entities*

After application of the equity method, the Group determines whether it is necessary to recognize any additional impairment loss with respect to the Group's net investment in the investee companies. The Group determines at each balance sheet date whether there is any objective evidence that the investment in the investee company is impaired. If this is the case, the Group calculates the amount of impairment as being the difference between the recoverable amount of the investee company and the carrying cost and recognizes the amount in the consolidated statement of income.

Goodwill

Goodwill acquired in a business combination is initially measured at cost being the excess of the cost of the business combination over the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities. After initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is reviewed for impairment, annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. Goodwill is included in the "Intangible assets" account in the consolidated balance sheet.

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the combination's synergies. Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units), to which the goodwill relates. Where the recoverable amount of the cash-generating unit is less than the carrying amount, an impairment loss is recognized. Where goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured on the basis of the relative values of the operation disposed of and the portion of the cash-generating unit retained.



### Provisions

Provisions are recognized when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the Group expects a provision to be reimbursed, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as interest expense. Provisions are reviewed at each balance sheet date and adjusted to reflect the current best estimate.

### Treasury Shares

Own equity instruments which are reacquired are carried at cost and are deducted from equity. No gain or loss is recognized in profit or loss on the purchase, sale, issue or cancellation of the Groups' own equity instruments. When the shares are retired, the capital stock account is reduced by its par value and the excess of cost over par value upon retirement is debited to additional paid-in capital to the extent of the specific or average additional paid-in capital when the shares were issued and to retained earnings for the remaining balance.

### Revenue and Cost Recognition

Revenue and cost from sales of completed projects by real estate subsidiaries is accounted for using the full accrual method. The percentage of completion method is used to recognize income from sales of projects where the subsidiaries have material obligations under the sales contracts to complete the project after the property is sold. Under this method, gain is recognized as the related obligations are fulfilled, measured principally on the basis of the estimated completion of a physical proportion of the contract work. Any excess of collections over the recognized receivables are included in the "Accounts payable and accrued expenses" account in the liabilities section of the consolidated balance sheet.

Revenue from construction contracts are recognized using the percentage of completion method, measured principally on the basis of the estimated physical completion of the contract work.

Contract costs include all direct materials and labor costs and those indirect costs related to contract performance. Expected losses on contracts are recognized immediately when it is probable that the total contract costs will exceed total contract revenue. Changes in contract performance, contract conditions and estimated profitability, including those arising from contract penalty provisions, and final contract settlements which may result in revisions to estimated costs and gross margins are recognized in the year in which the changes are determined.

Rent income from investment properties is recognized in the consolidated statement of income either on a straight-line basis over the lease term, or based on a certain percentage of the gross revenue of the tenants, as provided under the terms of the lease contract.

Revenue from sales of electronic products and vehicles are recognized when the significant risks and rewards of ownership of the goods have passed to the buyer and the amount of revenue can be measured reliably.



Revenue from hotel operations are recognized when services are rendered. Revenue from banquets and other special events are recognized when the events take place.

Revenue from internet operations are recognized when services are rendered and goods are delivered.

Management fees from administrative services, property management and other fees are recognized when services are rendered.

Interest is recognized as it accrues (using the effective interest method that is the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset).

Gain or loss is recognized in the statement of income if the Company disposes some of its investment in a subsidiary or associate. Gain or loss is computed as the difference between the proceeds of the disposal and its carrying amount, including the carrying amount of goodwill, if any.

Dividend income is recognized when the Group's right to receive payment is established.

#### Leases

Finance leases, which transfer substantially all the risks and benefits incidental to ownership of the leased item, are capitalized at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income.

Capitalized leased assets are depreciated over the shorter of the estimated useful lives of the assets or the respective lease terms.

Leases where the lessor retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Fixed lease payments are recognized on a straight-line basis over the lease term.

The determination of whether an arrangement is, or contains a lease is based on the substance of the arrangement at inception date of whether the fulfillment of the arrangement is dependent on the use of a specific asset or assets or the arrangement conveys a right to use the asset. A reassessment is made after inception of the lease only if one of the following applies: (a) there is a change in contractual terms, other than a renewal or extension of the arrangement; (b) a renewal option is exercised or extension granted, unless the term of the renewal or extension was initially included in the lease term; (c) there is a change in the determination of whether fulfillment is dependent on a specified asset; or (d) there is a substantial change to the asset.

Where a reassessment is made, lease accounting shall commence or cease from the date when the change in circumstances gave rise to the reassessment for scenarios (a), (c) or (d) and at the date of renewal or extension period for scenario (b).



### Commission Expense

Commissions paid to sales or marketing agents on the sale of pre-completed real estate units are deferred when recovery is reasonably expected and are charged to expense in the period in which the related revenue is recognized as earned. Accordingly, when the percentage of completion method is used, commissions are likewise charged to expense in the period the related revenue is recognized. Commission expense is included in the "Cost of sales and services" account in the consolidated statement of income.

### Borrowing Costs

Borrowing costs are generally expensed as incurred. Interest and other financing costs incurred during the construction period on borrowings used to finance property development are capitalized as part of development cost (included in real estate inventories, land and improvements, investment properties and property, plant and equipment). Capitalization of borrowing costs commences when the activities to prepare the asset are in progress and expenditures and borrowing costs are being incurred. The capitalization of these borrowing costs ceases when substantially all the activities necessary to prepare the asset for its intended use or sale are complete. If the carrying amount of the asset exceeds its recoverable amount, an impairment loss is recorded. Capitalized borrowing cost is based on the applicable weighted average borrowing rate from general borrowings and the actual borrowing costs eligible for capitalization for funds borrowed specifically.

Interest expense on loans is recognized using the effective interest rate method over the term of the loans.

### Pension Cost

Pension cost is actuarially determined using the projected unit credit method. This method reflects services rendered by employees up to the date of valuation and incorporates assumptions concerning employees' projected salaries. Actuarial valuations are conducted with sufficient regularity, with option to accelerate when significant changes to underlying assumptions occur. Pension cost includes current service cost, interest cost, expected return on any plan assets, actuarial gains and losses and the effect of any curtailments or settlements.

The liability recognized in the consolidated balance sheet in respect of the defined benefit plans is the present value of the defined benefit obligation at the balance sheet date less the fair value of the plan assets. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using risk-free interest rates that have terms to maturity approximating the terms of the related pension liability.

The net pension asset is the lower of the fair value of the plan assets less the present value of the defined benefit obligation at the balance sheet date, together with adjustments for unrecognized actuarial gains or losses and past service costs that shall be recognized in future periods, or the total of any cumulative unrecognized net actuarial losses and past service cost and the present value of any economic benefits available in the form of refunds from the plan or reductions in the future contributions to the plan.



Actuarial gains and losses is recognized as income or expense if the cumulative unrecognized actuarial gains and losses at the end of the previous reporting period exceeded the greater of 10% of the present value of defined benefit obligation or 10% of the fair value of plan assets. These gains or losses are recognized over the expected average remaining working lives of the employees participating in the plans.

#### Income Taxes

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantially enacted by the balance sheet date.

Deferred income tax is provided, using the balance sheet liability method, on all temporary differences, with certain exceptions, at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognized for all taxable temporary differences, with certain exceptions. Deferred tax assets are recognized for all deductible temporary differences, carryforward benefit of unused tax credits from excess of minimum corporate income tax (MCIT) over the regular corporate income tax and unused net operating loss carryover (NOLCO), to the extent that it is probable that taxable income will be available against which the deductible temporary differences and carryforward benefits of MCIT and NOLCO can be utilized.

Deferred tax liabilities are not provided on non-taxable temporary differences associated with investments in domestic subsidiaries, associates and interests in jointly controlled entities. With respect to investments in foreign subsidiaries, associates and interests in jointly controlled entities, deferred tax liabilities are recognized except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable income will be available to allow the deferred tax assets to be utilized. Unrecognized deferred tax assets are reassessed at each balance sheet date and are recognized to the extent that it has become probable that future taxable income will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period when the asset is realized or the liability is settled, based on tax rates and tax laws that have been enacted or substantially enacted at the balance sheet date.

Income tax relating to items recognized directly in equity is recognized in equity and not in the consolidated statement of income.

Deferred tax assets and deferred tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.



#### Foreign Currency Translation/Transactions

The functional and presentation currency of Ayala Corporation and its Philippine subsidiaries (except IMI), is the Philippine Peso (₱). Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency. Transactions in foreign currencies are initially recorded in the functional currency rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All differences are taken to the consolidated statement of income with the exception of differences on foreign currency borrowings that provide a hedge against a net investment in a foreign entity. These are taken directly to equity until the disposal of the net investment, at which time they are recognized in the consolidated statement of income. Tax charges and credits attributable to exchange differences on those borrowings are also dealt with in equity. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of initial transaction. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

The functional currency of BHL, IMI and AIPL is the US Dollar (\$). As at the reporting date, the assets and liabilities of these subsidiaries are translated into the presentation currency of the Group at the rate of exchange ruling at the balance sheet date and their statement of income are translated at the weighted average exchange rates for the year. The exchange differences arising on the translation are taken directly to a separate component of equity. On disposal of a foreign entity, the deferred cumulative amount recognized in equity relating to that particular foreign operation shall be recognized in the consolidated statement of income.

#### Share-based Payments

The Company and its subsidiaries have equity-settled, share-based compensation plans with its employees.

#### *PFRS 2 Options*

For options granted after November 7, 2002 that have not vested on or before January 1, 2005, the cost of equity-settled transactions with employees is measured by reference to the fair value at the date on which they are granted. In valuing equity-settled transactions, vesting conditions, including performance conditions, other than market conditions (conditions linked to share prices), shall not be taken into account when estimating the fair value of the shares or share options at the measurement date. Instead, vesting conditions are taken into account in estimating the number of equity instruments that will ultimately vest. The fair value is determined by using the Black-Scholes model, further details of which are provided in Note 25 to the consolidated financial statements.

The cost of equity-settled transactions is recognized, together with a corresponding increase in equity, over the period in which the performance conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award ('vesting date'). The cumulative expense recognized for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Group's best estimate of the number of equity instruments that will ultimately vest. The income or expense for a period represents the movement in cumulative expense recognized as at the beginning and end of that period.



No expense is recognized for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied.

Where the terms of an equity-settled award are modified, as a minimum, an expense is recognized as if the terms had not been modified. In addition, an expense is recognized for any increase in the value of the transaction as a result of the modification, as measured at the date of modification.

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognized for the award is recognized immediately. However, if a new award is substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award, as described in the previous paragraph.

#### *Pre-PFRS 2 Options*

For options granted before November 7, 2002 that have vested before January 1, 2005, the intrinsic value of stock options determined as of grant date is recognized as expense over the vesting period.

The dilutive effect of outstanding options is reflected as additional share dilution in the computation of diluted earnings per share (see Note 23).

#### *Employee Share Purchase Plans*

The Company and some of its subsidiaries have employee share purchase plan (ESOWN) which allows the grantees to purchase the Company and its respective subsidiaries' shares at a discounted price. The Group recognizes the difference between the market price at the time of subscription and the subscription price as stock compensation expense over the holding period. Where the subscription receivable is payable over more than one year, the subscription price is adjusted for the time value and treated as additional stock compensation expense. For the unsubscribed shares where the employees still have the option to subscribe in the future, these are accounted for as options.

#### Earnings Per Share

Basic earnings per share (EPS) is computed by dividing net income applicable to common stockholders by the weighted average number of common shares issued and outstanding during the year and adjusted to give retroactive effect to any stock dividends declared during the period. Diluted EPS is computed by dividing net income applicable to common stockholders by the weighted average number of common shares issued and outstanding during the year after giving effect to assumed conversion of dilutive potential common shares.

#### Segment Reporting

The Group's operating businesses are organized and managed separately according to the nature of the products and services provided, with each segment representing a strategic business unit that offers different products and serves different markets. Financial information on business segments is presented in Note 26 to the consolidated financial statements.



#### Contingencies

Contingent liabilities are not recognized in the consolidated financial statements. These are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote. Contingent assets are not recognized in the consolidated financial statements but disclosed when an inflow of economic benefits is probable.

#### Subsequent Events

Post year-end events that provide additional information about the Group's position at the balance sheet date (adjusting events) are reflected in the consolidated financial statements. Post year-end events that are not adjusting events are disclosed in the consolidated financial statements when material.

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### 3. **Significant Accounting Judgments and Estimates**

The preparation of the accompanying consolidated financial statements in conformity with PFRS requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. The estimates and assumptions used in the accompanying financial statements are based upon management's evaluation of relevant facts and circumstances as of the date of the financial statements. Actual results could differ from such estimates.

#### Judgments

In the process of applying the Group's accounting policies, management has made the following judgments, apart from those involving estimations, which have the most significant effect on the amounts recognized in the consolidated financial statements:

##### *Operating lease commitments - group as lessor*

The Group has entered into commercial property leases on its investment property portfolio. The Group has determined that it retains all significant risks and rewards of ownership of these properties which are leased out on operating leases.

##### *Distinction between investment properties and owner-occupied properties*

The Group determines whether a property qualifies as investment property. In making its judgment, the Group considers whether the property generates cash flows largely independent of the other assets held by an entity. Owner-occupied properties generate cash flows that are attributable not only to property but also to the other assets used in the production or supply process.

Some properties comprise a portion that is held to earn rentals or for capital appreciation and another portion that is held for use in the production or supply of goods or services or for administrative purposes. If these portions cannot be sold separately as of balance sheet date, the property is accounted for as investment property only if an insignificant portion is held for use in the production or supply of goods or services or for administrative purposes. Judgment is applied in determining whether ancillary services are so significant that a property does not qualify as investment property. The Group considers each property separately in making its judgment.



*Distinction between inventories and land and improvements*

The Group determines whether a property will be classified as real estate inventories or land and improvement. In making this judgment, the Group considers whether the property will be sold in the normal operating cycle (Real estate inventories) or whether it will be retained as part of the Group's strategic landbanking activities for development or sale in the medium or long-term (Land and improvements).

*Fair value of financial instruments*

Where the fair values of financial assets and financial liabilities recorded in the balance sheet cannot be derived from active markets, they are determined using internal valuation techniques using generally accepted market valuation models. The inputs to these models are taken from observable markets where possible, but where this is not feasible, estimates are used in establishing fair values. These judgments may include considerations of liquidity and model inputs such as correlation and volatility for longer dated derivatives.

*HTM investments*

The classification of HTM investments requires significant judgment. In making this judgment, the Group evaluates its intention and ability to hold such investments to maturity. If the Group fails to keep these investments to maturity other than in certain specific circumstances, it will be required to reclassify the entire portfolio as AFS investments. The investments would therefore be measured at fair value and not at amortized cost.

*Impairment of AFS equity investments*

The Group treats AFS equity investments as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is 'significant' or 'prolonged' requires judgment. The Group treats 'significant' generally as 20% or more and 'prolonged' as greater than 6 months for quoted equity securities. In addition, the Group evaluates other factors, including normal volatility in share price for quoted equities and the future cash flows and the discount factors for unquoted equities.

*Financial assets not quoted in an active market*

The Group classifies financial assets by evaluating, among others, whether the asset is quoted or not in an active market. Included in the evaluation on whether a financial asset is quoted in an active market is the determination on whether quoted prices are readily and regularly available, and whether those prices represent actual and regularly occurring market transactions on an arm's length basis.

*Contingencies*

The Group is currently involved in various legal proceedings. The estimate of the probable costs for the resolution of these claims has been developed in consultation with outside counsel handling the defense in these matters and is based upon an analysis of potential results. The Group currently does not believe that these proceedings will have a material effect on the Group's financial position. It is possible, however, that future results of operations could be materially affected by changes in the estimates or in the effectiveness of the strategies relating to these proceedings.



### Management's Use of Estimates

The key assumptions concerning the future and other sources of estimation and uncertainty at the balance sheet date that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

#### *Revenue and cost recognition*

ALI's revenue recognition policies require management to make use of estimates and assumptions that may affect the reported amounts of revenues and costs. ALI's revenue from real estate and construction contracts are recognized based on the percentage of completion measured principally on the basis of the estimated completion of a physical proportion of the contract work, and by reference to the actual costs incurred to date over the estimated total costs of the project.

#### *Estimating allowance for doubtful accounts*

The Group maintains allowance for doubtful accounts at a level based on the result of the individual and collective assessment under PAS 39. Under the individual assessment, the Group is required to obtain the present value of estimated cash flows using the receivable's original effective interest rate. Impairment loss is determined as the difference between the receivable's carrying balance and the computed present value. Factors considered in individual assessment are payment history, past due status and term. The collective assessment would require the Group to group its receivables based on the credit risk characteristics (customer type, payment history, past-due status and term) of the customers. Impairment loss is then determined based on historical loss experience of the receivables grouped per credit risk profile. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. The methodology and assumptions used for the individual and collective assessments are based on management's judgment and estimate. Therefore, the amount and timing of recorded expense for any period would differ depending on the judgments and estimates made for the year.

As of December 31, 2007 and 2006, allowance for doubtful accounts amounted to ₱442.4 million and ₱441.6 million, respectively (see Note 6). Accounts and notes receivables, net of allowance for doubtful accounts, amounted to ₱21.3 billion and ₱20.0 billion as of December 31, 2007 and 2006, respectively (see Note 6).

#### *Evaluation of asset impairment*

The Group reviews investments in associates and jointly controlled entities, investment properties, property, plant and equipment and intangible assets for impairment of value. Impairment for goodwill is assessed at least annually. This includes considering certain indications of impairment such as significant changes in asset usage, significant decline in assets' market value, obsolescence or physical damage of an asset, plans in the real estate projects, significant underperformance relative to expected historical or projected future operating results and significant negative industry or economic trends.

As described in the accounting policy, the Group estimates the recoverable amount as the higher of the net selling price and value in use. For goodwill, this requires an estimation of the recoverable amounts which is the net selling price or value in use of the cash-generating units to which the goodwill is allocated. In determining the present value of estimated future cash flows expected to be generated from the continued use of the assets, the Group is required to make



estimates and assumptions that may affect investments in associates and jointly controlled entities, investment properties, property, plant and equipment and intangible assets.

In determining the amount of impaired goodwill in 2007, the Group determined the recoverable amount of the investment in a subsidiary based on the estimated net selling price of the cash generating unit to which the goodwill is allocated. The excess of the carrying amount of the investment over the estimated net selling price is allocated first to the goodwill resulting in an impairment loss of ₱662.6 million (see Note 13).

Investments in associates and jointly controlled entities, investment properties, property, plant and equipment and intangible assets amounted to ₱100.7 billion and ₱98.9 billion as of December 31, 2007 and 2006, respectively (see Notes 9, 11, 12 and 13).

*Estimating useful lives of investment properties, property, plant and equipment, and intangible assets.*

The Group estimated the useful lives of its investment properties, property, plant and equipment and intangible assets based on the period over which the assets are expected to be available for use. The estimated useful lives of investment properties, property, plant and equipment and intangible assets are reviewed at least annually and are updated if expectations differ from previous estimates due to physical wear and tear and technical or commercial obsolescence on the use of these assets. It is possible that future results of operations could be materially affected by changes in these estimates brought about by changes in factors mentioned above. A reduction in the estimated useful lives would increase depreciation expense and decrease noncurrent assets.

Investment properties, property, plant and equipment and intangible assets amounted to ₱29.2 billion and ₱30.3 billion as of December 31, 2007 and 2006, respectively (see Notes 11, 12 and 13).

*Deferred tax assets*

The Group reviews the carrying amounts of deferred income taxes at each balance sheet date and reduces deferred tax assets to the extent that it is no longer probable that sufficient taxable income will be available to allow all or part of the deferred tax assets to be utilized. However, there is no assurance that the Group will generate sufficient taxable income to allow all or part of deferred tax assets to be utilized. The Group looks at its projected performance in assessing the sufficiency of future taxable income.

As of December 31, 2007 and 2006, the Group has net deferred tax assets amounting to ₱983.6 million and ₱1.1 billion, respectively. As of December 31, 2007 and 2006, the Group has net deferred tax liabilities amounting to ₱155.8 million and ₱443.7 million, respectively.

*Share-based payments*

The expected life of the options is based on the expected exercise behavior of the stock option holders and is not necessarily indicative of the exercise patterns that may occur. The volatility is based on the average historical price volatility which may be different from the expected volatility of the shares of stock of the Group.

Total expense arising from share-based payments recognized by the Group amounted to ₱288.0 million in 2007, ₱285.4 million in 2006 and ₱413.8 million in 2005.



*Estimating pension obligation and other retirement benefits*

The determination of the Group's obligation and cost of pension and other retirement benefits is dependent on the selection of certain assumptions used by actuaries in calculating such amounts. Those assumptions are described in Note 24 to the consolidated financial statements and include among others, discount rates, expected returns on plan assets and rates of salary increase. While the Group believes that the assumptions are reasonable and appropriate, significant differences in the actual experience or significant changes in the assumptions materially affect retirement obligations. See Note 24 to the consolidated financial statements for the related balances.

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#### 4. Cash and Cash Equivalents

This account consists of the following:

	2007	2006
	(In Thousands)	
Cash on hand and in banks	₱5,419,829	₱3,283,299
Cash equivalents	31,415,720	17,108,002
	<b>₱36,835,549</b>	<b>₱20,391,301</b>

Cash in banks earns interest at the prevailing bank deposit rates. Cash equivalents are short-term investments that are made for varying periods of up to three months depending on the immediate cash requirements of the Group, and earn interest at the respective short-term investment rates.

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#### 5. Short-term Investments

This account consists of the following:

	2007	2006
	(In Thousands)	
Money market placements	₱2,287,606	₱2,927,928
Investment Management Account (IMA)	1,400,000	-
	<b>₱3,687,606</b>	<b>₱2,927,928</b>

Money market placements are short-term investments made for varying periods of more than three months and up to six months and earn interest at the respective short-term investment rates.

The IMA is a six-month investment made through a Directional IMA with a local bank where funds are invested in special depository accounts with the Bangko Sentral ng Pilipinas (BSP).



## 6. Accounts and Notes Receivable

This account consists of the following:

	2007	2006
	(In Thousands)	
Trade:		
Real estate	₱9,412,522	₱7,817,166
Electronics manufacturing	2,972,599	3,233,505
Automotive	779,768	526,212
Information technology and business process outsourcing	362,238	253,064
International and others	66,943	64,151
Advances to other companies	2,231,057	2,280,965
Related parties (see Note 28)	2,395,624	1,935,112
Advances to contractors	1,394,106	675,504
Dividends	–	1,262,538
Others	2,133,846	2,382,796
	<b>21,748,703</b>	20,431,013
Less allowance for doubtful accounts	442,404	441,637
	<b>21,306,299</b>	19,989,376
Less noncurrent portion	4,010,373	2,519,816
	<b>₱17,295,926</b>	₱17,469,560

The classes of trade receivables of the Group are as follows:

### *Real estate*

Real estate receivables are receivables relating to the sale of large-scale fully integrated residential and commercial communities, residential and commercial lots and residential condominiums and office buildings; and the development and leasing of retail and office space. It also includes receivables from sale of industrial and business parks; development and sale of upper middle-income and affordable housing; hotel, cinema and theater operations; and construction and property management.

The sales contract receivables, included in real estate receivables, are collectible in monthly installments over a period of one to ten years and bear annual interest rates ranging from 2.5% to 18.0% computed on the diminishing balance of the principal. Titles to real estate properties are not transferred to the buyers until full payment has been made.

### *Electronics manufacturing*

Electronics manufacturing receivables pertain to receivables arising from manufacturing and other related services for electronic products and components and collectible within 30 to 45 days from invoice date.

### *Automotive*

Automotive receivables are receivables relating to manufacture and sale of passenger cars and commercial vehicles and are collectible within 30 to 90 days from date of sale.



*Information technology and business process outsourcing*

Information technology and business process outsourcing receivables arose from venture capital for technology businesses; provision of value-added content for wireless services, on-line business-to-business and business-to-consumer services; electronic commerce; and technology infrastructure sales and technology services; and onshore-and offshore-business process outsourcing services.

*International and others*

International and other receivables arose from investments in overseas property companies and projects, charter services, agri-business and others.

*Receivables from related parties and advances to other companies*

Receivable from related parties and advances to other companies are due and demandable.

*Advances to contractors*

Advances to contractors are recouped upon every progress billing payment depending on the percentage of accomplishment.



Movements in the allowance for doubtful accounts are as follows (in thousands):

2007							
	Real Estate	Electronics Manufacturing	Automotive	Information Technology and BPO	International and Others	Others	Total
At January 1	₱106,976	₱20,449	₱32,925	₱14,045	₱61,142	₱206,100	₱441,637
Provisions during the year	36,065	31,003	-	4,216	18	56,399	127,701
Translation adjustments	-	(6,167)	-	-	-	(543)	(6,710)
Write-offs	(22,818)	(13,308)	(6,818)	-	-	(75,411)	(118,355)
Reversals	(715)	(797)	-	-	-	(357)	(1,869)
At December 31	₱119,508	₱31,180	₱26,107	₱18,261	₱61,160	₱186,188	₱442,404
Individually impaired	₱32,119	₱31,180	₱-	₱18,261	₱60,134	₱185,462	₱327,156
Collectively impaired	87,389	-	26,107	-	1,026	726	115,248
Total	₱119,508	₱31,180	₱26,107	₱18,261	₱61,160	₱186,188	₱442,404
Gross amount of loans and receivables individually determined to be impaired, before deducting any individually assessed impairment allowance	₱32,119	₱31,180	₱-	₱18,261	₱60,134	₱232,256	₱373,950

2006							
	Real Estate	Electronics Manufacturing	Automotive	Information Technology and BPO	International and Others	Others	Total
At January 1	₱107,973	₱23,767	₱33,342	₱10,560	₱62,027	₱162,914	₱400,583
Provisions during the year	-	1,400	-	3,485	-	74,898	79,783
Translation adjustments	-	(1,705)	-	-	-	(220)	(1,925)
Write-offs	(997)	(3,013)	-	-	-	(13,987)	(17,997)
Reversals	-	-	(417)	-	(885)	(17,505)	(18,807)
At December 31	₱106,976	₱20,449	₱32,925	₱14,045	₱61,142	₱206,100	₱441,637
Individually impaired	₱19,587	₱20,449	₱-	₱14,045	₱61,142	₱205,374	₱320,597
Collectively impaired	87,389	-	32,925	-	-	726	121,040
Total	₱106,976	₱20,449	₱32,925	₱14,045	₱61,142	₱206,100	₱441,637
Gross amount of loans and receivables individually determined to be impaired, before deducting any individually assessed impairment allowance	₱19,587	₱20,449	₱-	₱14,045	₱61,142	₱205,374	₱320,597



As of December 31, 2007 and 2006, certain real estate receivables with a nominal amount of ₱5.7 billion and ₱4.7 billion, respectively, and receivable from employees with a nominal amount of ₱367.3 million and ₱301.2 million, respectively, were recorded initially at fair value. The fair value of the receivables was obtained by discounting future cash flows using the applicable rates of similar types of instruments. The unamortized discount amounted to ₱823.0 million and ₱756.0 million as of December 31, 2007 and 2006, respectively.

## 7. Inventories

This account consists of the following:

	2007	2006
	(In Thousands)	
Real estate inventories:		
Subdivision land for sale		
At cost	<b>₱3,487,850</b>	₱3,798,338
At NRV	<b>455,100</b>	455,100
Condominium, residential and commercial units for sale - at cost	<b>2,341,030</b>	3,070,123
Materials, supplies and others - at NRV (cost of ₱1,301,195 in 2007 and ₱1,142,846 in 2006)	<b>1,196,332</b>	1,029,214
Work-in-process - at cost	<b>294,558</b>	482,824
Vehicles - at cost	<b>719,766</b>	256,041
Finished goods - at cost	<b>228,151</b>	216,587
Parts and accessories - at NRV (cost of ₱146,468 in 2007 and ₱110,386 in 2006)	<b>119,748</b>	83,669
	<b>₱8,842,535</b>	₱9,391,896

Inventories recognized as cost of sales amounted to ₱34.4 billion and ₱33.8 billion in 2007 and 2006, respectively, and were included under costs of sales and services in the consolidated statement of income.

## 8. Other Current Assets

This account consists of the following:

	2007	2006
	(In Thousands)	
Prepaid expenses	<b>₱1,116,792</b>	₱534,398
FVPL financial assets	<b>622,097</b>	2,302,694
Value-added input tax	<b>621,653</b>	479,748
Derivative assets	<b>143,322</b>	-
Others	<b>593,756</b>	644,475
	<b>₱3,097,620</b>	₱3,961,315



FVPL financial assets consist of:

	2007	2006
	(In Thousands)	
Government securities	<b>₱318,018</b>	₱1,951,090
Investment securities	<b>304,079</b>	351,604
	<b>₱622,097</b>	₱2,302,694

Government securities pertain to treasury bonds and treasury bills that have a yield to maturity of 5.7% and 5.1% to 5.6% in 2007 and 2006, respectively. The Group recognized unrealized gain on these government securities amounting to ₱18.0 million and ₱43.8 million in 2007 and 2006, respectively.

As of December 31, 2007 and 2006, investment securities have a fair value of US\$7.4 million and US\$7.3 million, respectively. Investment securities include the Company's investment in The Rohatyn Group (TRG) Allocation LP. TRG Allocation LP's underlying asset is that of a fund that invests primarily in emerging market securities, including debt, equities and currencies.

As of December 31, 2007, derivative assets pertain to those of ALI and IMI. ALI has an outstanding nondeliverable forward contract with a notional amount of US\$25.0 million which will mature on October 30, 2008. Fair value gains amounted to ₱59.02 million. IMI has an outstanding structured currency option with a notional amount of US\$11.1 which will mature by December 31, 2008. Fair value gains amounted to ₱84.3 million.

#### Fair Value Changes on Derivatives

The net movements in fair value changes of the Group's derivative instruments in 2007 are as follows (amounts in thousands):

	Gain
Balance at beginning of year	₱-
Net changes in fair value of derivatives not designated as accounting hedges	227,841
	227,841
Fair value of settled instruments	84,519
Balance at end of year	₱143,322

## 9. Investments in Associates and Jointly Controlled Entities

This account consists of the following:

	2007	2006
	(In Thousands)	
Acquisition cost	<b>₱52,185,116</b>	₱49,424,793
Accumulated equity in net income	<b>18,035,250</b>	17,226,423
Cumulative translation adjustments	<b>1,339,891</b>	1,917,467
	<b>₱71,560,257</b>	₱68,568,683



The Group's equity in the net assets of its associates and jointly controlled entities and the related percentages of ownership are shown below.

	Percentage of Ownership		Carrying Amounts	
	2007	2006	2007	2006
Domestic:			(In Millions)	
Bank of the Philippine Islands and subsidiaries (BPI)	33.5**	33.9**	₱30,852	₱29,860
Globe Telecom, Inc. and subsidiaries (Globe)*	33.3	34.3	21,461	22,606
Manila Water Company, Inc. (MWCI)*	30.0**	30.0**	2,921	2,576
eTelecare Global Solutions, Inc. (eTelecare)	22.2**	—	2,753	—
Emerging City Holdings, Inc. (ECHI)*	50.0	50.0	2,485	2,233
Cebu Holdings, Inc. and subsidiaries (CHI)	47.2	47.2	1,810	1,724
North Triangle Depot Commercial Corporation (NTDCC)	49.0	49.0	1,541	1,044
Philwater Holdings Company, Inc. (Philwater)*	60.0	60.0	1,110	947
Berkshires Holdings, Inc. (BHI)*	50.0	50.0	1,065	957
Bonifacio Land Corporation	8.0	8.0	934	855
Asiacom Philippines, Inc. (Asiacom)*	60.0	60.0	794	747
Alabang Commercial Corporation (ACC)*	50.0	50.0	573	491
ALI Property Partners Holdings Corporation (APPHC)*	60.0	60.0	238	130
Foreign:				
Arch Asian Partners L.P.	19.4**	—	894	—
Glory High Investments Ltd. (Glory High)	40.0	—	563	—
Arch Capital Management Co. Ltd. (ARCH Capital)*	42.1**	55.7**	2	3,271
Others	Various	Various	1,564	1,128
			<b>₱71,560</b>	<b>₱68,569</b>

\* Jointly controlled entities.

\*\* Effective ownership interest of the Company.

The fair value of investments in associates for which there are published price quotations amounted to ₱61,587.9 million and ₱61,180.1 million as of December 31, 2007 and 2006, respectively.

Financial information on significant investees (amounts in millions, except earnings per share figures) follows:

BPI	2007	2006
Total resources	₱637,285	₱583,133
Total liabilities	566,154	517,646
Minority interest	1,120	1,048
Net interest income	18,950	19,196
Other income	13,604	10,641
Other expenses	18,311	16,663
Net income attributable to:		
Equity holders of the bank	10,012	9,040
Minority interests	214	154
Earnings per share		
Basic	3.78	3.34
Diluted	3.78	3.34



Globe	2007	2006
Current assets	<b>₱18,740</b>	₱24,215
Noncurrent assets	<b>97,880</b>	100,365
Total assets	<b>116,621</b>	124,580
Current liabilities	<b>27,600</b>	25,758
Noncurrent liabilities	<b>33,604</b>	41,874
Total liabilities	<b>61,204</b>	67,632
Net operating revenue	<b>68,042</b>	62,955
Costs and expenses	<b>47,991</b>	45,357
Net income	<b>13,277</b>	11,755
Earnings per share:		
Basic	<b>100.07</b>	88.56
Diluted	<b>99.58</b>	88.32
<b>MWCI</b>	<b>2007</b>	<b>2006</b>
Current assets	<b>₱4,122</b>	₱7,496
Noncurrent assets	<b>20,313</b>	16,766
Total assets	<b>24,435</b>	24,263
Current liabilities	<b>3,708</b>	4,399
Noncurrent liabilities	<b>7,363</b>	7,990
Total liabilities	<b>11,071</b>	12,389
Redeemable preferred stock	—	200
Revenue	<b>7,825</b>	6,785
Costs and expenses	<b>4,515</b>	4,559
Net income	<b>2,419</b>	2,394
Earnings per share:		
Basic	<b>1.06</b>	1.05
Diluted	<b>1.06</b>	1.05

The following significant transactions affected the Group's investment in its investees:

Investment in BPI

In 2007, BPI adopted the provisions of Pre-need Rule 31, As Amended, *Accounting Standards for Pre-need Plans and Pre-need Uniform Chart of Accounts*, as required by the SEC. As provided under SEC Interpretative Bulletin No. 1, Series of 2008, the impact of the adoption did not result in a restatement of BPI's prior year financial statements. The adjustment resulting from the transition to the Amended Pre-need Rule 31 amounting to ₱253.5 million was reflected in the opening balance of retained earnings as of January 1, 2007 of BPI. The Company's share in the said adjustment amounting to ₱85.0 million is reflected as a reduction in the January 1, 2007 retained earnings.

In 2006, the Company received 20% stock dividends from its investment in BPI.



#### Investment in Globe

In 2005, Globe offered to purchase one share for every fifteen shares (1:15) of its outstanding common stock from all stockholders of record as of February 10, 2005 at ₱950.00 per share. The buyback program allowed Globe to purchase up to 9,326,924 shares representing 6.67% of its outstanding common shares. Each shareholder was entitled to tender a proportionate number of shares at the 1:15 ratio for purchase by Globe upon and subject to the terms and conditions of the tender offer. The Company participated in the buyback program up to the number of shares it was allowed to tender.

The Company also holds 60% of Asiacom Philippines, Inc., which owns 158,515,021 Globe preferred shares. The Company does not exercise control over Asiacom since it is a joint venture with Singapore Telecom Inc.

#### Investment in eTelecare

In 2007, LiveIt acquired an additional 3.9 million common shares at a cost of ₱1.9 billion increasing its ownership interest in eTelecare from 11.2% to 22.2%. LiveIt accounted for its investment in eTelecare using the equity method from the date that eTelecare became an associate. In prior years, the investment in eTelecare amounting to ₱827.2 million is presented as part of “Investment in bonds and others securities” in the consolidated balance sheet (see Note 10).

#### Investment in NTDCC

In 2004, ALI acquired an additional 30.89% interest in NTDCC in exchange for ALI’s interest in two companies valued at ₱320.1 million and cash amounting to ₱280.0 million. ALI infused additional cash in NTDCC amounting to ₱112.0 million for an additional 1.85% equity interest in the latter.

A series of capital calls were made by NTDCC amounting to ₱484.8 million in 2007.

NTDCC was granted development rights by MRT Development Co. to construct and operate a commercial center under certain terms and conditions until the end of a 50-year lease term renewable for another 25 years. NTDCC officially started the construction of the shopping center in 2005 and became operational on May 16, 2007.

#### Investment in Philwater

On December 23, 2004, the Company entered into an agreement with Philwater to assign and transfer its 200.0 million participating preferred shares of MWCI in exchange for 60% ownership or 200.0 million common shares of Philwater. The assignment of shares became effective on January 31, 2005 when the SEC approved the increase in the authorized capital stock of Philwater and the assignment as payment by the Company of its subscription to such increase. The Company does not exercise control over Philwater since it is a joint venture with United Utilities Pacific Holdings BV.

#### Investment in APPHC

In 2006, ALI signed an agreement with MLT Investments Ltd. (MIL) and Filipinas Investments Ltd. (FIL) to jointly develop a BPO office building in Dela Rosa Street and to purchase the existing PeopleSupport Building.



APPHC, the newly formed joint-venture company, is 60% owned by ALI. The remaining 40% interest is split evenly between MIL and FIL. APPHC is jointly controlled by ALI, MIL, and FIL.

ALI has contributed a total capital of ₱232.7 million as of December 31, 2007.

#### Investment in ARCH Fund

In 2006, the Company and ALI entered into a Shareholders' Agreement with ARCH Capital and Great ARCH Co. Limited, wherein the Company and ALI committed to invest a total of US\$75.0 million in a private equity fund that will explore property markets in Asia, excluding Japan and Philippines. On the same year, an Amendment and Adherence Agreement was entered into by the same parties, together with Fine State Group Limited (Fine State) and Green Horizons Holdings Limited (Green Horizons), transferring the interests of the Company and ALI in ARCH Capital into Fine State and Green Horizons, respectively. Fine State and Green Horizons are effectively 100% owned Hong Kong subsidiaries of the Company and ALI, respectively.

The Company (through Fine State) and ALI (through Green Horizons) both have interests in the fund management company, ARCH Capital, which is tasked to raise third party capital and pursue investments for the Fund. As of December 31, 2007, the Company (through Fine State) and ALI (through Green Horizon) owned a combined interest in ARCH Capital of 50%.

In 2007, the private equity fund, called ARCH Asian Partners, L.P. (Fund) was established. As of December 31, 2007, the Fund achieved its final closing, resulting in a total investor commitment of US\$330.0 million. As a result, a portion of the funds disbursed by the Company and ALI which were invested into the Fund has been returned in 2007, reducing the Company and ALI's overall invested capital to ₱580.3 million as of December 31, 2007.

The Company and ALI exercise significant influence over the Fund by virtue of their interest in the general partner and in ARCH Capital. Accordingly, the Company and ALI account for their investments in the Fund using the equity method of accounting.

#### Investment in Glory High

In 2007, Fine State, a wholly owned subsidiary of Bestfull Holdings, Ltd., through Glory High entered into a consortium with ARCH Fund and certain Macau/Hong Kong investors-developers to develop an upper middle income residential community in Macau (Macau Project). As of December 31, 2007, total investment made by Fine State (through Glory High) to the Macau Project amounted to US\$13.6 million.

The excess of cost of investments over the Group's equity in the net assets of their investees accounted for under the equity method amounted to ₱10.8 billion and ₱10.9 billion as of December 31, 2007 and 2006, respectively.



## 10. Investments in Bonds and Other Securities

This account consists of investments in:

	2007	2006
	(In Thousands)	
AFS equity investments		
Quoted	<b>₱2,166,168</b>	₱2,373,486
Unquoted	<b>258,798</b>	961,374
	<b>2,424,966</b>	3,334,860
HTM investments		
Bonds	<b>67,947</b>	127,575
	<b>₱2,492,913</b>	₱3,462,435

The quoted equity investments include investments in TRG Global Opportunity Fund (GOF) and TRG Special Opportunity Fund (SOF). The GOF is a multi-strategy hedge fund which invests primarily in emerging markets securities. The SOF focuses on less liquid assets in emerging markets (Latin America, Asia, Emerging Europe, Middle East and Africa) such as distressed debt, NPLs, corporate high yield, mid and small cap stocks, real estate (debt and equity) and private equity.

Unquoted equity investments classified as AFS are carried at cost less any accumulated impairment losses, as their fair values cannot be reliably measured. As of December 31, 2006, the unquoted equity investments include an 11% minority stake in eTelecare. In 2007, the 11% stake in eTelecare, which has increased to a 22% stake, has been reclassified to "Investment in associates and jointly controlled entities" account (see Note 9). Unquoted investments in shares of stock includes unlisted preferred shares in a public utility company which the Group will continue to carry as part of the infrastructure that it provides for its real estate development projects.

As of December 31, 2006, the Company holds 124,137,930 MWCI preferred shares amounting to ₱124.1 million. On September 28, 2007, MWCI redeemed all of the preferred shares.

As of December 31, 2007, HTM investments pertain to fixed rate treasury notes that will mature on February 25, 2009 and bear effective interest rate of 11.4%. In prior years, HTM investments include investment in Globe Telecom bonds that will mature in 2012 and bear effective interest rate of 9.1%. Such investment was redeemed in 2007.

The rollforward of unrealized gain on AFS financial assets is as follows:

	2007	2006
	(In Thousands)	
Balance at beginning of year	<b>₱2,078,522</b>	₱477,839
Gain (loss) recognized in equity	<b>(343,837)</b>	2,487,563
Gain removed from equity and recognized in profit and loss	<b>(22,669)</b>	(886,880)
Balance at end of year	<b>₱1,712,016</b>	₱2,078,522



## 11. Investment Properties

The movements of investment properties follow:

	2007	2006
	(In Thousands)	
<b>Cost</b>		
At January 1	₱21,523,096	₱21,083,187
Additions	929,835	547,476
Transfers	1,149,756	649,594
Disposals	(906,248)	(757,161)
At December 31	22,696,439	21,523,096
<b>Accumulated depreciation and amortization and impairment losses</b>		
At January 1	4,728,434	4,071,348
Depreciation and amortization (see Note 20)	881,546	734,332
Reversal of impairment loss	(120,717)	(3,584)
Disposals	(208,997)	(73,662)
At December 31	5,280,266	4,728,434
<b>Net book value</b>	<b>₱17,416,173</b>	<b>₱16,794,662</b>

Certain parcels of land are leased to several individuals and corporations. Some of the lease contracts provide, among others, that within a certain period from the expiration of the contracts, the lessee will have to demolish and remove all improvements (such as buildings) introduced or built within the leased properties. Otherwise, the lessor will cause the demolition and removal thereof and charge the cost to the lessee unless the lessor occupies and appropriates the same for its own use and benefit.

The fair value of the investment properties has been determined based on valuations performed by independent professional qualified appraisers. The fair value represents the amount at which the assets could be exchanged between a knowledgeable, willing buyer and a knowledgeable, willing seller in an arm's length transaction at the date of valuation. The aggregate fair value of the Group's investment properties amounted to ₱123.8 billion in 2007 and ₱124.9 billion in 2006.

The value of the land and condominium units was arrived at using the *Market Data Approach*. In this approach, the value of the land and condominium units is based on sales and listings of comparable property registered within the vicinity. The technique of this approach requires the establishment of comparable property by reducing reasonable comparative sales and listings to a common denominator. This is done by adjusting the differences between the subject property and those actual sales and listings regarded as comparable. The properties used as basis of comparison are situated within the immediate vicinity of the subject property.

Consolidated rental income from investment properties amounted to ₱5.5 billion in 2007, ₱5.3 billion in 2006 and ₱4.2 billion in 2005. Consolidated direct operating expenses arising from the investment properties amounted to ₱2.4 billion in 2007, ₱2.1 billion in 2006 and ₱2.0 billion in 2005.



In 2007, ALI wrote-off investment properties (with net book value of ₱72.0 million) which were damaged during the Glorietta 2 explosion and other investment properties connected to the Ayala Center redevelopment amounting to ₱141.9 million.

## 12. Property, Plant and Equipment

The movements in property, plant and equipment follow:

	2007						
	Land, Buildings and Improvements (see Note 16)	Machinery and Equipment (see Note 27)	Hotel Property and Equipment (see Note 16)	Furniture, Fixtures and Equipment	Transportation Equipment	Construction-in-Progress	Total
	(In Thousands)						
<b>Cost</b>							
At January 1	₱3,435,033	₱6,327,518	₱2,702,209	₱2,068,901	₱937,686	₱952,377	₱16,423,724
Additions	141,277	885,535	29,511	156,172	184,712	1,904,972	3,302,179
Disposals	(190,745)	(156,141)	(38,651)	(119,797)	(81,788)	(23,802)	(610,924)
Transfers	22,042	(381,473)	–	(119,468)	(588)	(1,479,098)	(1,958,585)
At December 31	3,407,607	6,675,439	2,693,069	1,985,808	1,040,022	1,354,449	17,156,394
<b>Accumulated depreciation and amortization and impairment loss</b>							
At January 1	1,429,479	2,783,886	1,326,151	1,280,517	546,616	–	7,366,649
Depreciation and amortization for the year	357,986	893,756	111,231	318,620	137,584	–	1,819,177
Disposals	(27,335)	(305,283)	(37,952)	(83,395)	(68,312)	–	(522,277)
At December 31	1,760,130	3,372,359	1,399,430	1,515,742	615,888	–	8,663,549
<b>Net book value</b>	<b>₱1,647,477</b>	<b>₱3,303,080</b>	<b>₱1,293,639</b>	<b>₱470,066</b>	<b>₱424,134</b>	<b>₱1,354,449</b>	<b>₱8,492,845</b>
	2006						
	Land, Buildings and Improvements (see Note 16)	Machinery and Equipment (see Note 27)	Hotel Property and Equipment (see Note 16)	Furniture, Fixtures and Equipment	Transportation Equipment	Construction-in-Progress	Total
	(In Thousands)						
<b>Cost</b>							
At January 1	₱2,807,882	₱3,653,294	₱4,824,337	₱3,532,735	₱824,329	₱854,930	₱16,497,507
Additions	185,800	1,297,867	264,260	415,071	227,115	1,060,541	3,450,654
Addition through business combination	–	–	–	1,120	1,353	–	2,473
Disposals	(247,344)	(105,064)	(31,218)	(18,563)	(115,111)	(4,846)	(522,146)
Transfers	688,695	1,481,421	(2,355,170)	(1,861,462)	–	(958,248)	(3,004,764)
At December 31	3,435,033	6,327,518	2,702,209	2,068,901	937,686	952,377	16,423,724
<b>Accumulated depreciation and amortization and impairment loss</b>							
At January 1	1,257,544	1,933,196	1,850,516	1,026,467	512,230	–	6,579,953
Depreciation and amortization for the year	205,222	917,909	177,105	257,196	123,989	–	1,681,421
Disposals	(33,287)	(67,219)	(25,453)	(3,146)	(89,603)	–	(218,708)
Transfers	–	–	(676,017)	–	–	–	(676,017)
At December 31	1,429,479	2,783,886	1,326,151	1,280,517	546,616	–	7,366,649
<b>Net book value</b>	<b>₱2,005,554</b>	<b>₱3,543,632</b>	<b>₱1,376,058</b>	<b>₱788,384</b>	<b>₱391,070</b>	<b>₱952,377</b>	<b>₱9,057,075</b>

Depreciation and amortization expense on property, plant and equipment amounted to ₱1,819.2 million in 2007, ₱1,681.4 million in 2006 and ₱1,127.7 million in 2005 (see Note 20).

As of December 31, 2007, the Group has commitments of ₱1.9 billion relating to the completion of the construction-in-progress projects of ALI.



### 13. Intangible Assets

The movements in intangible assets follow:

	2007						Total
	Goodwill	Customer Relationships	Order Backlog	Unpatented Technology	Developed Software	Licenses	
(In Thousands)							
<b>Cost</b>							
At January 1	₱3,493,437	₱1,035,092	₱4,928	₱4,928	₱24,526	₱-	₱4,562,911
Addition through business combination (see Note 21)	317,100	-	-	-	-	-	317,100
Additions during the year	278	12,000	-	-	-	140,946	153,224
Exchange differences	(546,577)	(110,738)	(800)	(800)	(4,214)	-	(663,129)
At December 31	3,264,238	936,354	4,128	4,128	20,312	140,946	4,370,106
<b>Accumulated amortization and impairment loss</b>							
At January 1	-	127,142	4,928	986	-	-	133,056
Amortization (see Note 20)	-	320,923	-	926	11,551	-	333,400
Impairment loss (see Note 20)	662,591	-	-	-	-	-	662,591
Exchange differences	-	(33,578)	(800)	(260)	-	-	(34,638)
At December 31	662,591	414,487	4,128	1,652	11,551	-	1,094,409
<b>Net book value</b>	<b>₱2,601,647</b>	<b>₱521,867</b>	<b>₱-</b>	<b>₱2,476</b>	<b>₱8,761</b>	<b>₱140,946</b>	<b>₱3,275,697</b>

	2006						Total
	Goodwill	Customer Relationships	Order Backlog	Unpatented Technology	Developed Software	Licenses	
(In Thousands)							
<b>Cost</b>							
At January 1	₱2,300,742	₱684,861	₱5,309	₱5,309	₱-	₱-	₱2,996,221
Addition through business combination (see Note 21)	1,192,695	399,380	-	-	24,526	-	1,616,601
Exchange differences	-	(49,149)	(381)	(381)	-	-	(49,911)
At December 31	3,493,437	1,035,092	4,928	4,928	24,526	-	4,562,911
<b>Accumulated amortization and impairment loss</b>							
Amortization (see Note 20)	-	132,354	5,130	1,026	-	-	138,510
Exchange differences	-	(5,212)	(202)	(40)	-	-	(5,454)
At December 31	-	127,142	4,928	986	-	-	133,056
<b>Net book value</b>	<b>₱3,493,437</b>	<b>₱907,950</b>	<b>₱-</b>	<b>₱3,942</b>	<b>₱24,526</b>	<b>₱-</b>	<b>₱4,429,855</b>

### 14. Noncurrent Assets Held for Sale

In 2006, the Group had negotiations to sell its equity interests in Makati Property Ventures, Inc. (MPVI) and Hermill Investments Pte. Ltd. (Hermill).

AHI, together with Ocmador Philippines B. V., agreed to sell MPVI to DBS Trustee Ltd. (Trustee of Ascott Residence Trust) on March 22, 2007.

AIPL, through its 100%-owned Ayala International Holdings Limited (AIHL), entered into a Sale and Purchase Agreement (SPA) with Hotel Properties Limited (HPL) on January 17, 2007 for the sale of its 23.3% interest in Hermill, the holding company for The Forum Shopping Mall, a 17-storey retail-cum-office development along Orchard Road in Singapore. The consideration for AIHL's 23.3% stake is Singapore Dollars (SGD) 47 million. The SPA further provides that if,



within 3 years from the Completion Date of March 2007, Hermill is able to obtain approval from the Singapore government for the demolition and re-development of The Forum Shopping Mall, HPL shall pay AIHL SGD 3.5 million.

In 2007, the Group recognized a gain amounting to ₱598.7 million as a result of the consummation of the sale of MPVI and ₱26.0 million as a result of the Hermill sale (included in “Income associated with noncurrent assets held for sale”).

The results of MPVI for 2006 and 2005 are presented below:

	2006	2005
	(In Thousands)	
Sales and services	₱733,261	₱673,147
Interest, fees, investment and other income	12,871	12,177
	746,132	685,324
Cost of sales and services	339,457	304,054
Depreciation	102,446	102,673
General administrative expenses	23,475	42,661
Interest and other financing charges	39,527	47,283
Provision for income tax	85,969	57,974
	590,874	554,645
<b>Income associated with noncurrent assets held for sale</b>	<b>₱155,258</b>	<b>₱130,679</b>

The major classes of assets and liabilities of MPVI and Hermill classified as held for sale as of December 31, 2006 are as follows:

	At Carrying Amounts (In Thousands)
<b>ASSETS</b>	
Cash	₱324,362
Accounts and notes receivable - net	44,382
Inventories	4,407
Other current assets	5,446
Investment in joint venture	1,574,167
Property and equipment	1,679,153
Deferred tax assets	22,672
Other noncurrent assets	3,895
<b>Noncurrent assets held for sale</b>	<b>₱3,658,484</b>
<b>LIABILITIES</b>	
Accounts payable and accrued expenses	₱145,269
Income tax payable	45,167
Current portion of long-term debt	139,821
Long-term debt	138,843
<b>Liabilities directly associated with noncurrent assets held for sale</b>	<b>₱469,100</b>



Long-term debt comprises a fixed rate \$5.7 million bank loan having an effective rate of 8.55% repayable in full on September 15, 2008.

EPS on income associated with noncurrent assets held for sale attributable to equity holders of the Company follows:

	2007	2006	2005
	(In Thousands, except EPS figures)		
Income associated with noncurrent assets held for sale	<b>₱624,788</b>	₱155,258	₱130,679
Less: Income associated with noncurrent assets held for sale attributable to minority interests	<b>139,982</b>	108,681	91,475
	<b>484,806</b>	46,577	39,204
Weighted average number of common shares for basic EPS	<b>413,990</b>	413,045	412,057
Dilutive shares arising from stock options	<b>1,978</b>	2,029	1,668
Adjusted weighted average number of common shares for diluted EPS	<b>415,968</b>	415,074	413,725
Basic EPS	<b>₱1.17</b>	₱0.11	₱0.10
Diluted EPS	<b>₱1.17</b>	₱0.11	₱0.09

## 15. Accounts Payable and Accrued Expenses

This account consists of the following:

	2007	2006
	(In Thousands)	
Accounts payable	<b>₱13,289,481</b>	₱11,505,755
Accrued expenses	<b>6,558,775</b>	4,654,567
Dividends payable	<b>1,213,727</b>	964,931
Interest payable	<b>579,886</b>	824,086
Related parties (see Note 28)	<b>297,786</b>	132,204
Accrued personnel costs	<b>223,887</b>	118,906
Taxes payable	<b>38,682</b>	29,697
Retention payable	<b>32,577</b>	75,985
Accrued utilities	<b>26,366</b>	19,585
	<b>₱22,261,167</b>	₱18,325,716

Accounts payable and accrued expenses are noninterest-bearing and are normally settled on 15-to 60-day terms. Other payables are noninterest-bearing and are normally settled within one year.



## 16. Short-term and Long-term Debt

Short-term debt consists of:

	2007	2006
	(In Thousands)	
Philippine peso debt - with interest rates ranging from 3.4% to 9.0% per annum in 2007 and 6.1% to 7.8% per annum in 2006	<b>₱2,243,900</b>	₱1,688,220
Foreign currency debt - with interest rates ranging from 3.1% to 6.4% per annum in 2007 and 4.1% to 6.4% per annum in 2006	<b>390,248</b>	815,787
	<b>₱2,634,148</b>	₱2,504,007

The Philippine peso debt consists mainly of ALI and its subsidiaries' bank loans of ₱1,613.0 million and ₱1,556.0 million as of December 31, 2007 and 2006, respectively. These are unsecured peso-denominated short-term borrowings with interest rates ranging from 5.5% to 7.9% per annum in 2007 and 6.1% to 7.6% per annum in 2006.

The foreign currency debt consists mainly of IMI's loans from various banks with interest rates ranging from 3.13% to 3.42% in 2007 and 4.15% to 4.45% in 2006 and have maturity dates of 7 to 30 days from date of issue.

In 2005, IMI obtained an US\$80.0 million syndicated bridge loan facility from a foreign bank to finance the acquisition of the shares of Speedy-tech Electronics Ltd. (STEL). The loan is due within one year, with an interest rate per annum equal to the aggregate of 1.25% plus US\$ LIBOR, extendable by another year subject to the agreement between IMI and the foreign bank. IMI paid the loan when it matured in 2006.

Long-term debt consists of:

	2007	2006
	(In Thousands)	
The Company:		
Bank loans - with interest rates ranging from 4.5% to 5.6% per annum in 2007 and 5.3% to 11.0% per annum in 2006 and varying maturity dates up to 2013	<b>₱7,129,091</b>	₱6,294,697
Fixed Rate Corporate Notes (FXCNs) with interest rates ranging from 6.7% to 10.4% per annum and varying maturity dates up to 2014	<b>10,680,000</b>	7,190,000
Bonds		
Due 2012	<b>6,000,000</b>	-
Due 2009	-	7,000,000
Syndicated term loans with interest rates ranging from 10.6% to 12.0% per annum and varying maturity dates up to 2007	-	1,250,000
	<b>23,809,091</b>	21,734,697

(Forward)



	2007	2006
	(In Thousands)	
Subsidiaries:		
Loans from banks and other institutions:		
Foreign currency - with interest rates ranging from 6.0% to 15% per annum in 2007 and 5.9% to 12.8% per annum in 2006	<b>₱9,639,934</b>	₱8,154,932
Philippine peso - with interest rates ranging from 5.0% to 20% per annum in 2007 and 7.8% to 12.0% per annum in 2006	<b>2,866,532</b>	2,658,451
Bonds		
Due 2007	-	3,000,000
Due 2008	<b>2,000,000</b>	2,000,000
Due 2009	<b>80,470</b>	42,960
FXCNs		
8.125% Guaranteed Euro Notes	<b>5,421,438</b>	6,706,393
	<b>23,588,374</b>	26,142,736
	<b>47,397,465</b>	47,877,433
Less current portion	<b>9,512,760</b>	9,359,594
	<b>₱37,884,705</b>	₱38,517,839

*The Company*

While the Company's long-term loans are generally unsecured, due to certain regulatory constraints in the local banking system regarding loans to directors, officers, stockholders and related interest, some of the Company's credit facilities with a local bank are secured by shares of stock of a consolidated subsidiary with carrying value of ₱1,809.9 million and ₱2,794.2 million as of December 31, 2007 and 2006, respectively, in accordance with BSP regulations.

All credit facilities of the Company outside of this local bank are unsecured, and their respective credit agreements provide for this exception. The Company positions its deals across various currencies, maturities and product types to provide utmost flexibility in its financing transactions.

As of December 31, 2007, the Company has undrawn borrowing facilities from local banks amounting to ₱1.5 billion.

In 2007 and 2005, the Company issued FXCNs consisting of 5- and 7-year notes to various financial institutions with fixed interest rates of 6.7% per annum in 2007 and 8.1% to 10.4% per annum in 2005.

On November 22, 2007, the Company issued 6.8% Fixed Rate Bonds with an aggregate principal amount of ₱6.0 billion to mature in 2012. Prior to maturity, the Company may redeem in whole the outstanding bonds on the twelfth and sixteenth coupon payment date. The bonds have been rated "PRS Aaa" by the Philippine Ratings Services Corporation (PhilRatings).



In 2004, the Company issued 12.7% Fixed Rate Bonds with an aggregate principal amount of ₱7.0 billion to mature in 2009. Prior to maturity, the Company may redeem outstanding bonds on any coupon payment date beginning in 2007. The bonds have been rated “PRs Aaa” by PhilRatings. On October 7, 2007, the Company fully redeemed the bonds due in 2009 at a premium of 1.0075%.

#### *Subsidiaries*

##### Foreign Currency Debt

In 2003, the Company, through a wholly owned subsidiary, entered into 5-year loan with a commercial bank, with the Company as guarantor, for up to US\$120 million at a rate of 240 points over the 1-, 3- or 6-month LIBOR at the Company’s option, drawable in various tranches over a period of 12 months. The loan was prepaid in 2007.

In 2006, the Company, through a wholly owned subsidiary, extended for 3 years a loan with a foreign bank, with the Company as guarantor, for US\$20 million at a rate of 105 bps over 1-, 3- or 6-month US\$ LIBOR at the Company’s option.

In October 2007, the Company, through a wholly owned subsidiary, entered into a 5-year syndicated loan for US\$150.0 million at a rate of 71.4 points over the 1-, 3- or 6 month LIBOR at the Company’s option.

In 2006, IMI obtained a US\$40.0 million 5-year term clean loan from a local bank payable in a single balloon payment at the end of the loan term. The interest is repriced quarterly at the rate of 3-months LIBOR plus margin of 0.80% and is payable quarterly.

In 2006, IMI Singapore obtained a US\$40.0 million variable rate 5-year loan, repayable in 10 equal semi-annual installments of US\$4.0 million commencing on May 29, 2007 and maturing on May 29, 2012. The interest is repriced semi-annually at the LIBOR rate plus 0.75% quoted by the bank and is payable semi-annually.

##### Philippine Peso Debt

The Philippine Peso loans pertain to ALI subsidiaries’ loans that will mature on various dates up to 2014 with floating interest rates at 100 bps to 150 bps spread over benchmark 91-day, PDST-F or PDST-R1 and fixed interest rates of 7.8% to 12.7% per annum. Certain subsidiaries loans are secured by mortgages on real estate properties, hotel properties and equipment and leasehold rights with a total carrying value of ₱612.2 million and ₱653.0 million as of December 31, 2007 and 2006, respectively.

ALI pledged its investment in shares of stock of Station Square East Commercial Corporation (SSECC), ALI’s subsidiary, with a carrying value of ₱1.5 billion as of December 31, 2007 and 2006, as collateral to secure the latter’s bank loans.

##### 5-Year Bonds due 2007

In 2002, ALI issued ₱3.0 billion bonds due in 2007, with interest at 200 bps over benchmark 91-day T-Bills based on secondary market bids (PDST-F). These bonds were fully paid when it matured in April 2007.



#### 5-Year Bonds due 2008

In 2003, ALI issued ₱2.0 billion bonds due in 2008 with fixed and floating rate tranches. The fixed-rate bonds carry a coupon of 10.8% per annum and have a nominal principal amount of ₱1.0 billion. The floating rate bonds, also worth ₱1.0 billion, bear a margin of 125 bps over benchmark 91-day PDST-F and are repriced quarterly. These bonds have been rated “PRS Aaa” by Philratings.

#### Home Starter Bonds due 2009

In 2006, ALI launched its Homestarter Bonds of up to ₱169.2 million with fixed interest rate of 5% per annum. The Homestarter Bonds are being issued monthly in a series for a period of thirty six (36) months with final maturity in March 2009. On maturity date, the principal amount of the bond is redeemable with the accrued interest. Should the bondholder decide to purchase an Ayala Land property, he is entitled to an additional 10% of the aggregate face value of the bond as bonus credit which together with the principal and accrued interest can be applied as downpayment. As of end of 2007 and 2006, outstanding Homestarter Bonds amounted to ₱80.5 million and ₱43.0 million, respectively.

#### 5-, 7- and 10-year FXCNs due in 2011, 2013 and 2016

In 2006, ALI issued ₱3.0 billion FXCNs consisting of 5-, 7- and 10-year notes issued to various financial institutions and will mature on various dates up to 2016. The FXCNs bear fixed interest rates ranging from 7.3% to 7.8% per annum depending on the term of the notes.

#### 10-year FXCNs due 2012

In 2002, ALI issued 10-year FXCNs with fixed interest rate of 14.9% per annum due 2012. ALI may redeem all (but not in part) of the FXCNs on the 7th anniversary. As of December 31, 2007, ₱580.0 million of these bonds are outstanding.

#### Guaranteed Euro Notes

In 2003, the Company through a wholly owned subsidiary, issued an 8.1% Guaranteed Euro Notes, due 2008, amounting to US\$200 million at 99.5% of its face value.

The loan agreements on long-term debt of the Company and certain subsidiaries provide for certain restrictions and requirements with respect to, among others, payment of dividends, incurrence of additional liabilities, investments and guaranties, mergers or consolidations or other material changes in their ownership, corporate set-up or management, acquisition of treasury stock, disposition and mortgage of assets and maintenance of financial ratios at certain levels. These restrictions and requirements were complied with by the Group as of December 31, 2007 and 2006.

Total interest paid amounted to ₱3.8 billion in 2007, ₱5.4 billion in 2006 and ₱4.3 billion in 2005.

Interest capitalized by subsidiaries amounted to ₱3.4 million in 2007 and ₱186.5 million in 2006. The average capitalization rate is 0.14% and 8.19% in 2007 and 2006, respectively.



## 17. Other Noncurrent Liabilities

This account consists of the following:

	2007	2006
	(In Thousands)	
Deposits and deferred credits	<b>₱4,070,262</b>	₱3,809,082
Retentions payable	<b>1,117,079</b>	794,810
Other liabilities	<b>1,630,302</b>	1,537,173
	<b>₱6,817,643</b>	₱6,141,065

Deposits are recorded at fair value, which was obtained by discounting future cash flows using the applicable rates of similar types of instruments. The difference between the cash received and its fair value is included in “Deferred credits”.

## 18. Cumulative Redeemable Preferred Shares

The details as to the number of preferred shares of the Company follow:

	No. of Shares			
	Authorized		Issued and Outstanding	
	2007	2006	2007	2006
	(In Thousands)			
Preferred - ₱1 par value				
A	<b>900,000</b>	900,000	–	500,000
AA	<b>300,000</b>	300,000	–	–
	<b>1,200,000</b>	1,200,000	–	500,000

The preferred shares are nonvoting, nonparticipating, cumulative and redeemable. Such shares enjoy preference in case of liquidation but are excluded from the preemptive rights in the issuance of preferred and common shares. The preferred shares are identical in all respects, except that Preferred AA are redeemable on the fifth year from issue date while the Preferred A shares are redeemable at such time as may be determined by the BOD.

In 2004, the Company issued the equivalent of ₱1,500 million and ₱1,000 million Preferred A shares at an amount of ₱5 per share with a dividend rate of 10.4% and 10.5% per annum, respectively. These Preferred A shares were fully redeemed in 2007.

In 2003, the Company issued the equivalent of ₱2,000 million Preferred A shares at an amount of ₱5 per share. These Preferred A shares bear dividends at the rate of 10.6% per annum and were redeemed in 2006 at the end of three years from issue date.

In 2001, the Company issued an equivalent of ₱1,745 million and ₱1,000 million Preferred AA shares, respectively, at an amount of ₱5 per share. These Preferred AA issues bear dividends at a rate of the average 91-day T-Bill Rate payable quarterly and redeemable at the issue price. These preferred shares were redeemed in 2004 and 2006.



## 19. Equity

The details of the Company's common and equity preferred shares follow:

	Common shares			Preferred B shares	
	2007	2006	2005	2007	2006
	(In Thousands, except par value figures)				
Authorized shares	<b>600,000</b>	380,000	380,000	<b>58,000</b>	58,000
Par value per share	<b>₱50</b>	₱50	₱50	<b>₱100</b>	₱100
Issued and subscribed shares	<b>414,687</b>	344,854	343,493	<b>58,000</b>	58,000
Treasury shares	<b>324</b>	4	4	-	-

### Preferred shares

In February 2006, the BOD approved the reclassification of the unissued preferred shares and redeemed preferred shares of the Company into 58 million new class of Preferred B shares with a par value of ₱100 per share or an aggregate par value of ₱5,800 million. The new preferred shares, to be known as Preferred B shares, have the following features: (a) optional redemption by the Company; (b) issue value, dividend rate and declaration thereof to be determined by the BOD; (c) cumulative in payment of current dividends as well as any unpaid back dividends and non-participating in any other further dividends; (d) non-convertible into common shares; (e) preference over holders of common stock in the distribution of corporate assets in the event of dissolution and liquidation of the Company and in the payment of the dividend at the rate specified at the time of issuance; (f) non-voting except in those cases specifically provided by law; (g) no pre-emptive rights to any issue of shares, common or preferred; and; (h) reissuable when fully redeemed.

In July 2006, the Company filed a primary offer in the Philippines of its Preferred B shares at an offer price of ₱100 per share to be listed and traded on the Philippine Stock Exchange. The Preferred B shares are cumulative, nonvoting and redeemable at the option of the Company under such terms that the BOD may approve at the time of the issuance of shares and with a dividend rate of 9.4578% per annum. The Preferred B shares may be redeemed at the option of the Company starting in the fifth year.

On January 31, 2008, the BOD approved the re-issuance and reclassification of 1.2 billion redeemed Preferred A and AA shares with a par value of ₱1.00 per share (see Note 18) into 12.0 million new Preferred A shares with a par value of ₱100 per share with the same features as the existing Preferred B shares except on the issue price and dividend rate and the amendment of the Company's amended Articles of Incorporation to reflect the reclassification of the redeemed Preferred shares into new Preferred A shares.

### Common shares

On December 7, 2006, the BOD approved the increase of the authorized common capital stock from ₱19.0 billion divided into 380,000,000 shares to ₱30.0 billion divided into 600,000,000 shares with a par value of ₱50 per share. The BOD likewise approved the declaration of a 20% stock dividend to all common stockholders to be issued from the increased authorized capital stock. On April 30, 2007, the Company's application for increase in authorized common stock and stock dividends were approved by the SEC.



The common shares may be owned or subscribed by or transferred to any person, partnership, association or corporation regardless of nationality, provided that at anytime at least 60% of the outstanding capital stock shall be owned by citizens of the Philippines or by partnerships, associations or corporations 60% of the voting stock or voting power of which is owned and controlled by citizens of the Philippines.

The details of the Company's paid-up capital follow:

	Preferred Stock - B	Common Stock	Subscribed	Additional Paid-in Capital	Subscriptions Receivable	Total Paid-up Capital
(In Thousands)						
As of January 1, 2007	₱5,800,000	₱17,166,964	₱75,754	₱335,343	(₱240,113)	₱23,137,948
Exercise of ESOP/ESOWN	-	17,119	24,931	322,079	(96,267)	267,862
Stock dividend	-	3,449,584	-	-	-	3,449,584
As of December 31, 2007	₱5,800,000	₱20,633,667	₱100,685	₱657,422	(₱336,380)	₱26,855,394

	Preferred Stock - B	Common Stock	Subscribed	Additional Paid-in Capital	Subscriptions Receivable	Total Paid-up Capital
(In Thousands)						
As of January 1, 2006	₱-	₱17,137,083	₱37,544	₱118,643	(₱333,574)	₱16,959,696
Exercise of ESOP/ESOWN	-	29,881	38,210	216,700	93,461	378,252
Issuance of shares	5,800,000	-	-	-	-	5,800,000
As of December 31, 2006	₱5,800,000	₱17,166,964	₱75,754	₱335,343	(₱240,113)	₱23,137,948

	Common Stock	Subscribed	Additional Paid-in Capital	Subscriptions Receivable	Total Paid-up Capital
(In Thousands)					
As of January 1, 2005	₱17,124,360	₱37,544	₱35,551	(₱301,136)	₱16,896,319
Exercise of ESOP/ESOWN	12,723	-	83,092	(32,438)	63,377
As of December 31, 2005	₱17,137,083	₱37,544	₱118,643	(₱333,574)	₱16,959,696

The movements in the Company's outstanding number of common shares follow:

	2007	2006	2005
(In Thousands)			
At January 1	344,850	343,488	343,238
Stock dividends	68,992	-	-
Exercise of options	841	1,362	254
Treasury stock	(320)	-	(4)
	414,363	344,850	343,488

On September 10, 2007, the BOD approved the creation of a share buyback program involving ₱2.5 billion worth of common capital stock. As of December 31, 2007, the Company acquired 319,243 common shares at a total cost of ₱159.4 million.



Retained Earnings

Retained earnings include the accumulated equity in undistributed net earnings of consolidated subsidiaries, associates and jointly controlled entities accounted for under the equity method amounting to ₱29,824.0 million, ₱24,858.9 million and ₱18,487.9 million as of December 31, 2007, 2006 and 2005, respectively. These amounts are not available for dividend declaration until received in the form of dividends from the subsidiaries, associates and jointly controlled entities.

Retained earnings are further restricted for the payment of dividends to the extent of the cost of the common shares held in treasury consisting of 323,622 common shares as of December 31, 2007 and 4,379 common shares as of December 31, 2006 and 2005.

Dividends consist of the following:

	2007	2006	2005
	(In Thousands, except dividends per share)		
Dividends to common shares			
Cash dividends declared during the year	₱3,312,426	₱2,756,618	₱1,376,037
Cash dividends per share	₱8.00	₱8.00	₱4.00
Stock dividends	₱3,449,584	-	-
Proposed for approval at annual stockholders' meeting	20% stock dividend	20% stock dividend	-
Dividends to equity preferred shares declared during the year	₱548,552	₱274,276	-

On January 31, 2008, the BOD approved the declaration of a 20% stock dividend to all common share holders of the Company as of a record date to be approved at the annual stockholders' meeting.

Cumulative translation adjustments are used to record exchange differences arising from the translation of the financial statements of foreign subsidiaries. It is also used to record the Group's share of the associates' equity reserve on fluctuation in value of investments.

Capital Management

The primary objective of the Company's capital management policy is to ensure that it maintains a strong credit rating and healthy capital ratios in order to support its business and maximize shareholder value.

The Company manages its capital structure and makes adjustments to it, in light of changes in economic conditions. To maintain or adjust the capital structure, the Company may adjust the dividend payment to shareholders or issue new shares. No changes were made in the objectives, policies or processes for the years ended December 31, 2007 and 2006.

The Company is not subject to externally imposed capital requirements.



The Company monitors capital using a gearing ratio of debt to equity and net debt to equity. Debt consists of short-term and long-term debt and redeemable preferred shares. Net debt includes short-term and long-term debt and redeemable preferred shares less cash and cash equivalents and short-term investments. The Company considers as capital the equity attributable to equity holders of the Company.

	2007	2006
	(In Thousands)	
Short-term debt	<b>₱2,634,148</b>	₱2,504,007
Long-term debt	<b>47,397,465</b>	47,877,433
Redeemable preferred shares	-	2,500,000
Total debt	<b>50,031,613</b>	52,881,440
Less:		
Cash and cash equivalents	<b>36,835,549</b>	20,391,301
Short-term investments	<b>3,687,606</b>	2,927,928
Net debt	<b>9,508,458</b>	29,562,211
Equity attributable to equity holders of the Company	<b>87,175,835</b>	77,135,527
Debt to equity	<b>57%</b>	69%
Net debt to equity	<b>11%</b>	38%

## 20. Other Income and Costs and Expenses

Other income consists of:

	2007	2006	2005
	(In Thousands)		
Gain on sale of investments	<b>₱8,844,822</b>	₱5,542,090	₱4,585,890
Foreign exchange gain (loss)	<b>795,581</b>	72,424	(4,662)
Management and marketing fees	<b>485,802</b>	590,066	382,050
Dividend income	<b>73,500</b>	180,250	95,774
Others	<b>528,670</b>	613,179	889,407
	<b>₱10,728,375</b>	₱6,998,009	₱5,948,459

Gain on sale of investments consists mostly of gain arising from the sale of the Company's investments in listed subsidiary, associate and jointly controlled entities.

In December 2007, ALI entered into a joint venture with Kingdom Hotel Investments, Inc. to develop a 7,377-square meter property along Makati Avenue corner Arnaiz Avenue (formerly Pasay Road) into a luxury hotel complex comprising a 300-room Fairmont Hotel, a 30-suite Raffles Hotel and 189 Raffles branded private residences. The total project cost is approximately US\$153.0 million.

The 7,377-square meter property to be developed was conveyed by ALI to KHI-ALI Manila, Inc. (KAMI) in exchange for 37,250 common shares, 38,250 redeemable preferred shares A and 16,758 preferred shares of ALI.



On December 13, 2007, ALI sold 16,758 of its preferred shares in KAMI to Kingdom Manila B.V., which resulted in a gain of ₱1,004.0 million, reported under “Gain on sale of investments” account.

Depreciation and amortization expense included in the consolidated statement of income are as follows:

	2007	2006	2005
	(In Thousands)		
Included in:			
Cost of sales and services	<b>₱1,971,932</b>	₱1,960,042	₱1,243,495
General and administrative expenses	<b>1,016,947</b>	630,316	471,182
	<b>₱2,988,879</b>	₱2,590,358	₱1,714,677

Personnel costs included in the consolidated statement of income are as follows:

	2007	2006	2005
	(In Thousands)		
Included in:			
Cost of sales and services	<b>₱4,495,767</b>	₱3,432,411	₱2,759,998
General and administrative expenses	<b>4,168,554</b>	3,959,265	3,110,135
	<b>₱8,664,321</b>	₱7,391,676	₱5,870,133

General and administrative expenses included in the consolidated statement of income are as follows:

	2007	2006	2005
	(In Thousands)		
Personnel costs (see Notes 24, 25 and 28)	<b>₱4,168,554</b>	₱3,959,265	₱3,110,135
Depreciation and amortization	<b>1,016,947</b>	630,316	471,182
Professional fees	<b>796,979</b>	574,881	375,825
Taxes and licenses	<b>530,583</b>	349,229	240,930
Transportation and travel	<b>376,087</b>	347,977	246,878
Rental and utilities	<b>357,666</b>	253,519	157,090
Advertising and promotions	<b>234,330</b>	158,455	129,398
Research and development	<b>189,693</b>	48,561	49
Supplies	<b>161,459</b>	111,509	58,515
Postal and communication	<b>153,649</b>	126,733	93,234
Entertainment, amusement and recreation	<b>141,782</b>	188,911	123,474
Repairs and maintenance	<b>132,257</b>	81,239	79,487
Provision for doubtful accounts (see Note 6)	<b>127,701</b>	79,783	101,418
Donations and contributions	<b>126,541</b>	106,969	99,927
Dues and fees	<b>61,033</b>	65,381	64,819
Insurance	<b>59,703</b>	45,088	39,319
Contract labor	<b>36,952</b>	23,051	20,405
Others	<b>826,390</b>	557,294	599,239
	<b>₱9,498,306</b>	₱7,708,161	₱6,011,324



Interest expense and other financing charges consist of:

	2007	2006	2005
		(In Thousands)	
Long-term debt	<b>₱3,506,030</b>	₱4,160,169	₱3,630,831
Short-term debt	<b>321,891</b>	512,997	845,377
Dividends on preferred shares	<b>154,335</b>	291,681	556,351
Amortization of discount on long-term debt - net of accretion of premium	<b>38,458</b>	59,205	134,571
Swap costs	-	-	176,303
Others	<b>99,446</b>	-	-
	<b>₱4,120,160</b>	₱5,024,052	₱5,343,433

Other charges consists of:

	2007	2006	2005
		(In Thousands)	
Write-offs and other charges	<b>₱669,949</b>	₱-	₱-
Impairment loss on goodwill	<b>662,591</b>	-	-
Provision for decline/writedown of assets	-	217,580	1,915,740
Others	<b>237,404</b>	169,339	303,560
	<b>₱1,569,944</b>	₱386,919	₱2,219,300

Write-offs and other charges include the write-down of investment properties damaged by the Glorietta 2 explosion and related expenses incurred and the demolition and relocation costs as part of ALI's redevelopment programs amounting to ₱213.7 million.

## 21. Business Combination

IFRS 3 provides that if the initial accounting for a business combination can be determined only provisionally by the end of the period in which the combination is effected because either the fair values to be assigned to the acquiree's identifiable assets, liabilities or contingent liabilities or the cost of the combination can be determined only provisionally, the acquirer shall account for the combination using those provisional values. The acquirer shall recognize any adjustments to those provisional values as a result of completing the initial accounting within twelve months of the acquisition date as follows: (i) the carrying amount of the identifiable asset, liability or contingent liability that is recognized or adjusted as a result of completing the initial accounting shall be calculated as if its fair value at the acquisition date had been recognized from that date; (ii) goodwill or any gain recognized shall be adjusted by an amount equal to the adjustment to the fair value at the acquisition date of the identifiable asset, liability or contingent liability being recognized or adjusted; and (iii) comparative information presented for the periods before the initial accounting for the combination is complete shall be presented as if the initial accounting has been completed from the acquisition date.



*2007 Acquisitions*

In February 2007, Integreon Managed Solutions, Inc. (Integreon), a wholly owned subsidiary of Integreon Inc. which in turn is a subsidiary of LiveIt, entered into a Stock Purchase Agreement with CBF Group, Inc. (CBF) and the sole shareholder of CBF for the purchase of all 100,000 issued and outstanding common shares of stock of CBF.

The purchase price allocation has been prepared on a preliminary basis and reasonable changes are expected as additional information becomes available.

*2006 Acquisitions*

On October 7, 2006, Conoda, Inc. (now Integreon, Inc.), a subsidiary of LiveIt, entered into an Agreement and Plan of Merger with Integreon for the purchase of all Integreon shares. The amount of US\$18.0 million was put in Integreon.

On December 15, 2006, Next Life, Inc. (now Affinity Holdings, Inc.), a subsidiary of LiveIt, entered into an Agreement and Plan of Merger with Affinity, Inc. (Affinity) for the purchase of all Affinity shares. The amount of US\$28.3 million was put in Affinity.

The purchase price allocation has been prepared on a preliminary basis, and reasonable changes are expected as additional information becomes available. The following is a summary of the provisional fair values of the assets acquired and liabilities assumed as of the date of the acquisition:

	Fair Value Recognized on Acquisition
	(In Thousands)
Cash and cash equivalents	₱83,719
Trade and other receivables	202,485
Other current assets	5,189
Property, plant and equipment - net	222,380
Intangible asset	95,239
Other noncurrent assets	692
	<u>609,704</u>
Accounts payable and accrued expenses	181,028
Other current liabilities	152,104
Other noncurrent liabilities	71,065
	<u>404,197</u>
Net assets	205,507
Minority interests	(97,297)
Goodwill arising on acquisition (see Note 13)	1,616,601
Total consideration, satisfied by cash	<u>₱1,724,811</u>

Cash flow on acquisition follows:

Net cash acquired with the subsidiary	₱83,719
Cash paid	1,724,811
Net cash outflow	<u>₱1,641,092</u>



From the date of acquisition, Integreon has contributed ₱188.2 million loss to the net income of the Group. If the contribution had taken place at the beginning of the year, the net income for the Group would have decreased by ₱169.9 million and revenue would have increased by ₱522.5 million in 2006. No income was recorded from Affinity since the business combination was completed in December 2006.

In 2007, LiveIt completed the valuation of the intangible assets which were part of the business combination. The fair values of the intangible assets are as follows (in thousands):

Intangible Assets	Integreon	Affinity
Customer relationships	₱88,510	₱310,870
Technology developed software	24,526	-
	<b>₱113,036</b>	<b>₱310,870</b>

Accordingly, the 2006 comparative information has been restated to reflect this adjustment. The value of customer relationships and developed software increase by ₱399.4 million and ₱24.5 million, respectively. There was also a corresponding reduction in goodwill by ₱423.9 million.

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## 22. Income Taxes

The components of the Group's deferred taxes as of December 31, 2007 and 2006 are as follows:

### *Net Deferred Tax Assets*

	2007	2006
	(In Thousands)	
Deferred tax assets on:		
Allowance for probable losses	<b>₱686,007</b>	₱687,949
Unrealized gain, deposits and accruals for various expenses on real estate transactions	<b>391,709</b>	518,619
Retirement benefits	<b>188,718</b>	192,177
Share-based payments	<b>47,541</b>	174,679
NOLCO	<b>19,007</b>	51,242
MCIT	<b>7,670</b>	17,780
Others	<b>386,976</b>	168,082
	<b>1,727,628</b>	1,810,528
Deferred tax liabilities on:		
Capitalized customs duties, interest and other expenses	<b>(723,404)</b>	(686,616)
Others	<b>(20,659)</b>	-
	<b>(744,063)</b>	(686,616)
<b>Net deferred tax assets</b>	<b>₱983,565</b>	<b>₱1,123,912</b>



*Net Deferred Tax Liabilities*

	2007	2006
	(In Thousands)	
Deferred tax assets on:		
Unrealized gain, deposits and accruals for various expenses on real estate transactions	<b>₱59,756</b>	₱58,070
NOLCO	<b>49,026</b>	47,967
Others	<b>9,232</b>	25,835
	<b>118,014</b>	131,872
Deferred tax liabilities on:		
Excess of financial realized gross profit over taxable realized gross profit	<b>(123,808)</b>	(244,113)
Capitalized customs duties, interest and other expenses	<b>(122,673)</b>	(290,728)
Others	<b>(27,289)</b>	(40,767)
	<b>(273,770)</b>	(575,608)
<b>Net deferred tax liabilities</b>	<b>(₱155,756)</b>	<b>(₱443,736)</b>

The Group has NOLCO amounting to ₱8.0 billion and ₱8.8 billion in 2007 and 2006, respectively, which were not recognized. Further, deferred tax assets from the excess MCIT over regular corporate income tax amounting to ₱37.1 million in 2007 and ₱28.8 million in 2006 and from unrealized gain on real estate sales amounting to ₱4.8 million and ₱143.3 million as of December 31, 2007 and 2006, respectively, were also not recognized. Deferred tax assets are recognized only to the extent that taxable income will be available against which the deferred tax assets can be used. The Group will recognize a previously unrecognized deferred tax asset to the extent that it becomes probable that future taxable income will allow the deferred tax asset to be recovered.

As of December 31, 2007, NOLCO and MCIT that can be claimed as deduction from future taxable income or used as deductions against income tax liabilities are as follows:

Year incurred	Expiry date	NOLCO	MCIT
(In Thousands)			
2005	2008	₱3,120,245	₱16,620
2006	2009	3,004,989	15,449
2007	2010	2,095,519	20,248
		<b>₱8,220,753</b>	<b>₱52,317</b>

At December 31, 2007 and 2006, deferred tax liabilities have not been recognized on the undistributed earnings and cumulative translation adjustment of foreign subsidiaries, associates and jointly controlled entities since the timing of the reversal of the temporary difference can be controlled by the Group and management does not expect the reversal of such temporary difference in the foreseeable future. Such undistributed earnings and cumulative translation adjustment amounted to ₱1,338.6 million and ₱1,417.2 million as of December 31, 2007 and 2006, respectively.

There are no income tax consequences attaching to the payment of dividends by the domestic subsidiaries, associates and jointly controlled entities to the Group.



Republic Act (RA) No. 9337

RA No. 9337 was recently enacted into law amending various provisions in the existing 1997 National Internal Revenue Code. Among the reforms introduced by the said RA, which became effective on November 1, 2005, are as follows:

- Increase in the corporate income tax rate from 32% to 35% with a reduction thereof to 30% beginning January 1, 2009;
- Increase in value added tax (VAT) rate from 10% to 12%, effective February 1, 2006 as authorized by the Philippine president pursuant to the recommendation of the Secretary of Finance;
- Revised invoicing and reporting requirements for VAT; and
- Expanded scope of transactions subject to VAT.

The reconciliation between the statutory and the effective income tax rates follows:

	2007	2006	2005
Statutory income tax rate	<b>35.00%</b>	35.00%	32.50%
Tax effects of:			
Gain on sale of shares and capital gains tax	<b>(17.56)</b>	(13.98)	(14.41)
Nontaxable equity in net earnings of associates and joint ventures	<b>(16.70)</b>	(17.84)	(24.69)
Interest income subjected to final tax at lower rates	<b>(1.82)</b>	(1.15)	(0.64)
Income under income tax holiday	<b>(0.04)</b>	0.16	(4.23)
Others	<b>10.81</b>	9.40	20.28
Effective income tax rate	<b>9.69%</b>	11.59%	7.77%

### 23. Earnings Per Share

The following table presents information necessary to calculate EPS on net income attributable to equity holders to the Company:

	2007	2006	2005
	(In Thousands, except EPS figures)		
Net income	<b>₱16,197,557</b>	₱12,176,771	₱8,198,004
Less dividends on preferred stock	<b>548,552</b>	274,276	-
	<b>₱15,649,005</b>	₱11,902,495	₱8,198,004
Weighted average number of common shares	<b>413,990</b>	413,045	412,057
Dilutive shares arising from stock options	<b>1,978</b>	2,029	1,668
Adjusted weighted average number of common shares for diluted EPS	<b>415,968</b>	415,074	413,725
Basic EPS	<b>₱37.80</b>	₱28.82	₱19.90
Diluted EPS	<b>₱37.62</b>	₱28.68	₱19.82



EPS on income before income associated with noncurrent assets held for sale attributable to equity holders of the Company follows:

	2007	2006	2005
	(In Thousands, except EPS figures)		
Income before income associated with noncurrent assets held for sale	<b>₱18,378,297</b>	₱14,312,367	₱9,959,445
Less: Income before income associated with noncurrent assets held for sale associated to minority interests	<b>2,665,546</b>	2,182,173	1,800,645
Less: Dividends on preferred stock	<b>548,552</b>	274,276	-
	<b>₱15,164,199</b>	₱11,855,918	₱8,158,800
Weighted average number of common shares for basic EPS	<b>413,990</b>	413,045	412,057
Dilutive shares arising from stock options	<b>1,978</b>	2,029	1,668
Adjusted weighted average number of common shares for diluted EPS	<b>415,968</b>	415,074	413,725
Basic EPS	<b>₱36.63</b>	₱28.70	₱19.80
Diluted EPS	<b>₱36.46</b>	₱28.56	₱19.72

#### 24. Retirement Plan

The Company and certain subsidiaries have their respective funded, noncontributory tax-qualified defined benefit type of retirement plans covering substantially all of their employees. The benefits are based on defined formula with minimum lump-sum guarantee of 1.5 months effective salary per year of service. The consolidated retirement costs charged to operations amounted to ₱331.5 million in 2007, ₱319.5 million in 2006 and ₱447.2 million in 2005.

The principal actuarial assumptions used to determine the pension benefits with respect to the discount rate, salary increases and return on plan assets were based on historical and projected normal rates. The Company's and certain subsidiaries' annual contributions to their respective plans consist of payments covering the current service cost for the year and the required funding relative to the guaranteed minimum benefits as applicable.

The components of pension expense in the consolidated statement of income are as follows:

	2007	2006	2005
	(In Thousands)		
Current service cost	<b>₱260,685</b>	₱239,923	₱356,998
Interest cost on benefit obligation	<b>158,528</b>	240,125	180,617
Expected return on plan assets	<b>(167,940)</b>	(163,718)	(84,858)
Net actuarial loss (gain)	<b>(18,715)</b>	4,362	(8,264)
Past service cost	<b>98,539</b>	1,466	2,706
Effect of ceiling limit	<b>357</b>	(2,642)	-
Total retirement expense	<b>₱331,454</b>	₱319,516	₱447,199
Actual return on plan assets	<b>₱244,109</b>	₱295,694	₱110,636



The funded status and amounts recognized in the consolidated balance sheet for the pension plan assets of subsidiaries in a net pension asset position as of December 31, 2007 and 2006 are as follows:

	2007	2006
	(In Thousands)	
Benefit obligation	<b>(₱683,176)</b>	(₱778,671)
Plan assets	<b>817,507</b>	782,711
	<b>134,331</b>	4,040
Unrecognized net actuarial loss	<b>6,657</b>	198,614
Unrecognized past service cost	<b>(412)</b>	-
Effect of ceiling limit	-	(56)
<b>Assets recognized in the consolidated balance sheet</b>	<b>₱140,576</b>	<b>₱202,598</b>

The funded status and amounts recognized in the consolidated balance sheet for the pension plan liabilities of the Company and subsidiaries in a net pension liability position as of December 31, 2007 and 2006 are as follows:

	2007	2006
	(In Thousands)	
Benefit obligation	<b>(₱3,025,722)</b>	(₱3,233,979)
Plan assets	<b>2,916,832</b>	2,484,639
	<b>(108,890)</b>	(749,340)
Unrecognized net actuarial losses (gains)	<b>(460,983)</b>	261,614
Unrecognized past service cost	<b>38,321</b>	-
<b>Liabilities recognized in the consolidated balance sheet</b>	<b>(₱531,552)</b>	<b>(₱487,726)</b>

Changes in the present value of the combined defined benefit obligation are as follows:

	2007	2006
	(In Thousands)	
Balance at January 1	<b>₱4,012,650</b>	₱3,026,065
Interest cost on benefit obligation	<b>158,528</b>	240,125
Current service cost	<b>260,685</b>	239,923
Benefits paid	<b>(291,372)</b>	(170,833)
Actuarial losses (gains) on obligations	<b>(569,821)</b>	675,904
Past service cost	<b>138,228</b>	1,466
<b>Balance at December 31</b>	<b>₱3,708,898</b>	<b>₱4,012,650</b>



Changes in the fair value of the combined plan assets are as follows:

	2007	2006
	(In Thousands)	
Balance at January 1	₱3,267,350	₱2,910,036
Expected return	167,940	163,718
Contributions by employer	273,039	234,321
Benefits paid	(291,372)	(170,833)
Actuarial gains on plan assets	317,382	130,108
Balance at December 31	₱3,734,339	₱3,267,350

The assumptions used to determine pension benefits for the Group are as follows:

	2007	2006
Discount rates	7.0 to 12.0%	7.0 to 11.9%
Salary increase rates	5.0 to 10.0%	5.0 to 10.0%
Expected rates of return on plan assets	3.3 to 10.0%	7.0 to 10.0%

The allocation of the fair value of plan assets of the Group follows:

	2007	2006
Investments in debt securities	63.6%	61.0%
Investments in equity securities	29.0%	35.0%
Others	7.4%	4.0%

Amounts for the current and previous annual periods are as follows:

	2007	2006	2005
	(In Thousands)		
Defined benefit obligation	(₱3,708,898)	(₱4,012,650)	(₱3,026,065)
Plan assets	3,734,339	3,267,350	2,910,036
Excess (deficit)	₱25,441	(₱745,300)	(₱116,029)

Experience adjustments on plan liabilities amounted to ₱136.6 million gain in 2007 and ₱41.8 million loss in 2006. Experience adjustment on plan assets amounted to ₱30.7 million gain in 2007 and ₱131.8 million gain in 2006.

The Company expects to contribute ₱58.3 million to its defined benefit pension plan in 2008.

As of December 31, 2007 and 2006, the plan assets include shares of stock of the Company with total fair value of ₱614.0 million and ₱764.6 million, respectively.

The overall expected rate of return on assets is determined based on the market prices prevailing on that date.



## 25. Stock Option Purchase Plans

The Company has stock option plans for the key officers (Executive Stock Option Plan - ESOP) and employees (Employee Stock Ownership Plan - ESOWN) covering 3.0% of the Company's authorized capital stock. The grantee is selected based on certain criteria like outstanding performance over a defined period of time.

The ESOP grantees may exercise in whole or in part the vested allocation in accordance with the vesting percentage and vesting schedule stated in the ESOP. Also, the grantee must be an employee of the Company or any of its subsidiaries during the 10-year option period. In case the grantee retires, he is given 3 years to exercise his vested and unvested options. In case the grantee resigns, he is given 90 days to exercise his vested options.

### ESOP

A summary of the Company's stock option activity and related information for the years ended December 31, 2007, 2006 and 2005 follows:

	2007		2006		2005	
	Number of Shares	Weighted Average Exercise Price	Number Of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
Outstanding, at beginning of year	2,533,908	₱205.13	3,785,816	₱202.56	4,400,110	₱203.90
Granted	-	-	-	-	31,530	295.00
Exercised	(169,656)	203.37	(1,251,908)	(197.35)	(645,819)	(212.14)
Cancelled	-	-	-	-	(5)	-
Adjustment due to 20% stock dividends (see Note 19)	472,850	-	-	-	-	-
Outstanding, at end of year	2,837,102	₱170.30	2,533,908	₱205.13	3,785,816	₱202.56

The options have a contractual term of 10 years. As of December 31, 2007 and 2006, the weighted average remaining contractual life of options outstanding is 5.2 years and 6.3 years, respectively, and the range of exercise prices amounted from ₱128.75 to ₱245.83.

The fair value of each option is estimated on the date of grant using the Black-Scholes option-pricing model. The fair values of stock options granted under ESOP at each grant date and the assumptions used to determine the fair value of the stock options are as follows:

	June 30, 2005	June 10, 2004
Weighted average share price	₱327.50	₱244.00
Exercise price	₱295.00	₱220.00
Expected volatility	46.78%	46.71%
Option life	10 years	10 years
Expected dividends	1.27%	1.43%
Risk-free interest rate	12.03%	12.75%

The expected volatility reflects the assumption that the historical volatility is indicative of future trends, which may also necessarily be the actual outcome.



## ESOWN

The Company also has ESOWN granted to qualified officers and employees wherein grantees may subscribe in whole or in part to the shares awarded to them based on the 10% discounted market price as offer price set at grant date. To subscribe, the grantee must be an employee of the Company or any of its subsidiaries during the 10-year payment period. In case the grantee resigns, unsubscribed shares are cancelled, while the subscription may be paid up to the percent of holding period completed and payments may be converted into the equivalent number of shares. In case the grantee is separated, not for cause, but through retrenchment and redundancy, subscribed shares may be paid in full, unsubscribed shares may be subscribed, or payments may be converted into the equivalent number of shares. In case the grantee retires, the grantee may subscribe to the unsubscribed shares anytime within the 10-year period. The plan does not allow sale or assignment of the shares. All shares acquired through the plan are subject to the Company's Right to Repurchase.

Shares granted under the ESOWN follows:

	2007	2006
Granted	623,335	772,227
Subscribed	619,912	767,955
Exercise price	₱400.00	₱320.00

Subscriptions receivable from the stock option plans covering the Company's shares are presented under equity.

Total expense arising from share-based payments recognized by the Group in the consolidated statement of income amounted to ₱288.0 million in 2007, ₱285.4 million in 2006 and ₱413.8 million in 2005.

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## 26. Segment Information

Business segment information is reported on the basis that is used internally for evaluating segment performance and deciding how to allocate resources among operating segments. Accordingly, the primary segment reporting format is by business segment. Secondary information is reported geographically.

The industry segments where the Group operates are as follows:

- Real estate and hotels - planning and development of large-scale fully integrated residential and commercial communities; development and sale of residential, leisure and commercial lots and the development and leasing of retail and office space and land in these communities; construction and sale of residential condominiums and office buildings; development of industrial and business parks; development and sale of upper middle-income and affordable housing; strategic land bank management; hotel, cinema and theater operations; and construction and property management.



- Financial services and bancassurance- universal banking operations, including savings and time deposits in local and foreign currencies; commercial, consumer, mortgage and agribusiness loans; leasing; payment services, including card products, fund transfers, international trade settlement and remittances from overseas workers; trust and investment services including portfolio management, unit funds, trust administration and estate planning; fully integrated bancassurance operations, including life, non-life, pre-need and reinsurance services; internet banking; on-line stock trading; corporate finance and consulting services; foreign exchange and securities dealing; and safety deposit facilities.
- Telecommunications - provider of digital wireless communications services, wireline voice communication services, consumer broadband services, other wireline communication services, domestic and international long distance communication or carrier services and mobile commerce services.
- Electronics, information technology and business process outsourcing services - electronics manufacturing services provider for original equipment manufacturers in the computing, communications, consumer, automotive, industrial and medical electronics markets; venture capital for technology businesses; provision of value-added content for wireless services, on-line business-to-business and business-to-consumer services; electronic commerce; and technology infrastructure hardware and software sales and technology services; and onshore- and offshore-business process outsourcing services.
- Water utilities - contractor to manage, operate, repair, decommission, and refurbish all fixed and movable assets (except certain retained assets) required to provide water delivery services and sewerage services in the East Zone Service Area.
- Automotive - manufacture and sale of passenger cars and commercial vehicles.
- International - investments in overseas property companies and projects.
- Others - air-charter services, agri-business and others.

The Group generally accounts for inter-segment sales and transfers as if the sales or transfers were to third parties at current market prices.



## Business Segments

The following tables regarding business segments present assets and liabilities as of December 31, 2007 and 2006 and revenue and profit information for each of the three years in the period ended December 31, 2007 (in millions).

### 2007

	Parent Company	Real Estate and Hotels	Electronics, Information Technology and Business Process Outsourcing Services	International	Automotive and Others	Consolidated
<b>Revenue</b>						
Sales to external customers	₱–	₱22,962	₱21,655	₱–	₱11,961	₱56,578
Equity in net earnings of investees*	8,638	804	(28)	226	68	9,708
Interest income	903	597	77	114	2	1,693
Other income	8,670	1,464	186	143	265	10,728
<b>Total revenue</b>	<b>18,211</b>	<b>25,827</b>	<b>21,890</b>	<b>483</b>	<b>12,296</b>	<b>78,707</b>
Operating expenses	1,819	17,970	20,798	242	11,838	52,667
<b>Operating profit</b>	<b>16,392</b>	<b>7,857</b>	<b>1,092</b>	<b>241</b>	<b>458</b>	<b>26,040</b>
Interest expense	(2,993)	(868)	(234)	(9)	(16)	(4,120)
Other expenses	(2)	(874)	(685)	–	(10)	(1,571)
Provision for income tax	(140)	(1,579)	(166)	(23)	(63)	(1,971)
<b>Income before income associated with noncurrent assets held for sale</b>	<b>13,257</b>	<b>4,536</b>	<b>7</b>	<b>209</b>	<b>369</b>	<b>18,378</b>
<b>Income associated with noncurrent assets held for sale, net of tax</b>	<b>–</b>	<b>599</b>	<b>–</b>	<b>26</b>	<b>–</b>	<b>625</b>
<b>Net income</b>	<b>₱13,257</b>	<b>₱5,135</b>	<b>₱7</b>	<b>₱235</b>	<b>₱369</b>	<b>₱19,003</b>
Net income attributable to:						
Equity holders of Ayala Corporation	₱13,259	₱2,815	(₱473)	₱230	₱367	₱16,198
Minority interests	(2)	2,320	480	5	2	2,805
	₱13,257	₱5,135	₱7	₱235	₱369	₱19,003
<b>Other Information</b>						
Segment assets	₱26,419	₱75,361	₱16,359	₱3,127	₱2,610	₱123,876
Investment in associates and jointly controlled entities	56,143	9,034	3,142	435	2,806	71,560
Deferred tax assets	–	929	31	24	–	984
<b>Total assets</b>	<b>₱82,562</b>	<b>₱85,324</b>	<b>₱19,532</b>	<b>₱3,586</b>	<b>₱5,416</b>	<b>₱196,420</b>
Segment liabilities	₱41,522	₱31,899	₱6,572	₱1,334	₱151	₱81,478
Deferred tax liabilities	–	114	26	7	9	156
<b>Total liabilities</b>	<b>₱41,522</b>	<b>₱32,013</b>	<b>₱6,598</b>	<b>₱1,341</b>	<b>₱160</b>	<b>₱81,634</b>
Segment additions to property, plant and equipment and investment properties	172	3,283	1,456	–	104	5,015
Depreciation and amortization	89	1,558	1,251	4	80	2,982
Non-cash expenses other than depreciation and amortization	₱291	₱267	₱688	₱–	₱–	₱1,246

\*Equity in net earnings of financial services, telecommunications and water utilities amounted to ₱3,291 million, ₱4,546 million and ₱741 million, respectively.



2006

	Parent Company	Real Estate and Hotels	Electronics, Information Technology and Business Process Outsourcing Services	International	Automotive and Others	Consolidated
<b>Revenue</b>						
Sales to external customers	₱-	₱23,805	₱20,557	₱-	₱9,032	₱53,394
Equity in net earnings of investees*	7,930	291	(25)	48	9	8,253
Interest income	771	659	55	31	5	1,521
Other income	5,040	1,054	337	390	177	6,998
<b>Total revenue</b>	13,741	25,809	20,924	469	9,223	70,166
Operating expenses	1,700	18,952	18,806	174	8,933	48,565
<b>Operating profit</b>	12,041	6,857	2,118	295	290	21,601
Interest expense	(3,895)	(813)	(286)	(21)	(9)	(5,024)
Other expenses	(49)	(281)	(49)	-	(8)	(387)
Provision for income tax	(54)	(1,633)	(116)	(23)	(51)	(1,877)
<b>Income before income associated with noncurrent assets held for sale</b>	8,043	4,130	1,667	251	222	14,313
<b>Income associated with noncurrent assets held for sale, net of tax</b>	-	155	-	-	-	155
<b>Net income</b>	₱8,043	₱4,285	₱1,667	₱251	₱222	₱14,468
Net income attributable to:						
Equity holders of Ayala Corporation	₱8,044	₱2,466	₱1,195	250	₱222	₱12,177
Minority interests	(1)	1,819	472	1	-	2,291
	₱8,043	₱4,285	₱1,667	₱251	₱222	₱14,468
<b>Other Information</b>						
Segment assets	₱17,164	₱70,686	₱19,390	₱3,761	₱1,638	₱112,639
Investment in associates and jointly controlled entities	55,598	8,791	200	3,614	366	68,569
Deferred tax assets	-	1,053	30	-	41	1,124
<b>Total assets</b>	₱72,762	₱80,530	₱19,620	₱7,375	₱2,045	₱182,332
Segment liabilities	₱40,386	₱30,410	₱8,180	₱471	₱607	₱80,054
Deferred tax liabilities	-	416	21	2	5	444
<b>Total liabilities</b>	₱40,386	₱30,826	₱8,201	₱473	₱612	₱80,498
Segment additions to property, plant and equipment and investment properties	68	2,263	1,523	3	144	4,001
Depreciation and amortization	92	1,402	1,013	4	79	2,590
Non-cash expenses other than depreciation and amortization	₱311	₱236	₱72	₱-	₱-	₱619

\*Equity in net earnings of financial services, telecommunications and water utilities amounted to ₱3,300 million, ₱4,109 million and ₱588 million, respectively.



2005

	Parent Company	Real Estate and Hotels	Electronics, Information Technology and Business Process Outsourcing Services	International	Automotive and Others	Consolidated
<b>Revenue</b>						
Sales to external customers	₱-	₱16,522	₱10,297	₱-	₱7,819	₱34,638
Equity in net earnings of investees*	8,043	176	(62)	45	-	8,202
Interest income	566	1,112	45	22	9	1,754
Other income	1,691	3,559	119	433	146	5,948
<b>Total revenue</b>	10,300	21,369	10,399	500	7,974	50,542
Operating expenses	1,518	13,675	9,293	220	7,475	32,181
<b>Operating profit</b>	8,782	7,694	1,106	280	499	18,361
Interest expense	(4,548)	(781)	(3)	(6)	(5)	(5,343)
Other expenses	(51)	(2,136)	(26)	(1)	(6)	(2,220)
Provision for income tax	(79)	(721)	(10)	(7)	(22)	(839)
<b>Income before income associated with noncurrent assets held for sale</b>	4,104	4,056	1,067	266	466	9,959
<b>Income associated with noncurrent assets held for sale, net of tax</b>	-	131	-	-	-	131
<b>Net income</b>	₱4,104	₱4,187	₱1,067	₱266	₱466	₱10,090
Net income attributable to:						
Equity holders of Ayala Corporation	₱4,105	₱2,606	₱755	₱266	₱466	₱8,198
Minority interests	(1)	1,581	312	-	-	1,892
	₱4,104	₱4,187	₱1,067	₱266	₱466	₱10,090

\*Equity in net earnings of financial services, telecommunications and water utilities amounted to ₱3,026 million, ₱3,616 million and ₱1,438 million, respectively.

## Geographical Segments

	Revenue		Segment Assets		Investment Properties and Property and Equipment Additions	
	2007	2006	2007	2006	2007	2006
	(In Thousands)					
Philippines	₱56,872,624	₱49,122,467	₱179,723,801	₱160,794,635	₱4,156,480	₱3,228,580
Japan	9,400,556	10,649,162	5,470	-	1,946	-
USA	6,081,976	4,801,189	6,477,017	9,088,035	329	271,789
Europe	3,525,576	3,149,512	-	-	-	-
Others (Mostly Asia)	2,827,080	2,443,665	10,213,197	12,449,234	856,628	499,924
	₱78,707,812	₱70,165,995	₱196,419,485	₱182,331,904	₱5,015,383	₱4,000,293

Summarized financial information of BPI, Globe and MWCI are presented in Note 9 to the consolidated financial statements.



## 27. Leases

### Finance leases - as lessee

Foreign subsidiaries conduct a portion of their operations from leased facilities, which include office equipment. These leases are classified as finance leases and expire over the next 5 years. The average discount rate implicit in the lease is 8.5% per annum in 2007 and 2006. Future minimum lease payments under the finance leases together with the present value of the net minimum lease payments are as follows:

	2007		2006	
	Minimum payments	Present values of payments	Minimum payments	Present values of payments
	(In Thousands)			
Within one year	<b>₱2,541</b>	<b>₱2,359</b>	₱6,054	₱6,021
After one year but not more than five years	<b>483</b>	<b>470</b>	2,207	2,183
Total minimum lease payments	<b>3,024</b>	<b>2,829</b>	8,261	8,204
Less amounts representing finance charges	<b>195</b>	-	57	-
Present value of minimum lease payments	<b>₱2,829</b>	<b>₱2,829</b>	₱8,204	₱8,204

### Operating lease commitments - as lessee

Future minimum rentals payable under non-cancellable operating leases of lessee subsidiaries are as follows:

	2007	2006
	(In Thousands)	
Within one year	<b>₱146,620</b>	₱105,956
After one year but not more than five years	<b>483,373</b>	523,576
More than five years	<b>1,577,925</b>	1,516,421
	<b>₱2,207,918</b>	₱2,145,953

### Operating leases - as lessor

Certain subsidiaries have lease agreements with third parties covering real estate properties. These leases generally provide for either (a) fixed monthly rent, or (b) minimum rent or a certain percentage of gross revenue, whichever is higher.

Future minimum rentals receivable under non-cancellable operating leases of the Group are as follows:

	2007	2006
	(In Thousands)	
Within one year	<b>₱653,150</b>	₱586,617
After one year but not more than five years	<b>1,485,316</b>	2,083,551
More than five years	<b>245,132</b>	300,048
	<b>₱2,383,598</b>	₱2,970,216



## 28. Related Party Transactions

The Group, in its regular conduct of business, has entered into transactions with associates, jointly controlled entities and other related parties principally consisting of advances and reimbursement of expenses, purchase and sale of real estate properties, various guarantees, construction contracts, and development, management, underwriting, marketing and administrative service agreements. Sales and purchases of goods and services to and from related parties are made at normal market prices.

The effects of the foregoing are shown under the appropriate accounts in the consolidated financial statements as follows:

2007				
	Income	Costs and Expenses	Amounts Owed by Related Parties	Amounts Owed to Related Parties
(In Thousands)				
Associates and joint ventures	₱343,267	₱2,202,909	₱1,307,627	₱286,000
Key management personnel	-	668,885	285,514	-
Other related parties	80,881	113,793	802,483	11,786
	<b>₱424,148</b>	<b>₱2,985,587</b>	<b>₱2,395,624</b>	<b>₱297,786</b>

2006				
	Income	Costs and Expenses	Amounts Owed by Related Parties	Amounts Owed to Related Parties
(In Thousands)				
Associates and joint ventures	₱619,858	₱6,374,376	₱1,391,917	₱47,187
Key management personnel	-	767,588	254,288	-
Other related parties	12,567	61,956	1,551,445	85,017
	<b>₱632,425</b>	<b>₱7,203,920</b>	<b>₱3,197,650</b>	<b>₱132,204</b>

2005				
	Income	Costs and Expenses	Amounts Owed by Related Parties	Amounts Owed to Related Parties
(In Thousands)				
Associates and joint ventures	₱575,676	₱3,980,618	₱774,680	₱55,174
Key management personnel	-	583,174	212,444	-
Other related parties	205,863	147,800	1,166,086	142,238
	<b>₱781,539</b>	<b>₱4,711,592</b>	<b>₱2,153,210</b>	<b>₱197,412</b>



Amounts owed by related parties include promissory notes issued by Bonifacio Land Corporation (BLC), which were assigned by Metro Pacific Corporation (MPC) to ALI and Evergreen Holdings Inc. (EHI) and the advances subsequently made by ALI to Fort Bonifacio Development Corporation (FBDC) to fund the completion of the Bonifacio Ridge project and to BLC to finance the costs to be incurred in relation to its restructuring program. These notes and advances are due and demandable and bear interest at the rate of 12% to 14% per annum.

Allowance for doubtful accounts to related parties amounted to ₱105.5 million and ₱111.4 million as of December 31, 2007 and 2006, respectively. Provision for doubtful accounts amounted to ₱1.7 million in 2007, ₱6.5 million in 2006 and ₱3.1 million in 2005.

Compensation of key management personnel by benefit type follows:

	2007	2006	2005
		(In Thousands)	
Short-term employee benefits	₱449,419	₱500,413	₱327,584
Share-based payments (see Note 25)	144,511	182,877	148,033
Post-employment benefits	74,955	84,298	107,557
	<b>₱668,885</b>	<b>₱767,588</b>	<b>₱583,174</b>

## 29. Financial Instruments

### *Fair Value of Financial Instruments*

The table below presents a comparison by category of carrying amounts and estimated fair values of all of the Group's financial instruments (in thousands):

	2007		2006	
	Carrying Value	Fair Value	Carrying Value	Fair Value
<b>FVPL FINANCIAL ASSETS</b>				
Financial assets at FVPL	₱622,097	₱622,097	₱2,302,694	₱2,302,694
Derivative assets	143,322	143,322	-	-
Total FVPL financial assets	<b>765,419</b>	<b>765,419</b>	2,302,694	2,302,694
<b>LOANS AND RECEIVABLES</b>				
Cash and cash equivalents	36,835,549	36,835,549	20,391,301	20,391,301
Short-term investments	3,687,606	3,687,606	2,927,928	2,927,928
Accounts and notes receivables				
Trade receivables				
Real estate	9,293,014	9,532,729	7,710,190	8,172,583
Electronics manufacturing	2,941,419	2,941,419	3,213,056	3,213,056
Information technology and business process outsourcing	343,977	343,977	239,018	239,018
Automotive	753,661	753,661	493,287	493,287
International and others	5,783	5,783	3,010	3,010
Total trade receivables	<b>13,337,854</b>	<b>13,577,569</b>	11,658,561	12,120,954

(Forward)



	2007		2006	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Nontrade receivables				
Advances to other companies	₱2,231,057	₱2,216,427	₱2,280,965	₱2,280,965
Receivable from related parties	2,395,624	2,395,624	1,935,112	1,935,112
Dividend receivables	–	–	1,262,538	1,262,538
Other receivables	1,947,658	1,927,833	2,176,696	2,176,696
Total nontrade receivables	6,574,339	6,539,884	7,655,311	7,655,311
Total loans and receivables	60,435,348	60,640,608	42,633,101	43,095,494
<b>AFS FINANCIAL ASSETS</b>				
Quoted shares of stocks	2,166,168	2,166,168	2,373,486	2,373,486
Unquoted shares of stocks	258,798	258,798	961,374	961,374
Total AFS investments	2,424,966	2,424,966	3,334,860	3,334,860
<b>HTM INVESTMENTS</b>				
Quoted debt investments	67,947	72,685	127,575	140,995
Total financial assets	₱63,693,680	₱63,903,678	₱48,398,230	₱48,874,043
<b>OTHER FINANCIAL LIABILITIES</b>				
Current Other Financial Liabilities				
Accounts payable and accrued expenses				
Accounts payable	₱13,289,481	₱13,289,481	₱11,505,755	₱11,505,755
Accrued expenses	6,558,775	6,558,775	4,654,567	4,654,567
Dividends payable	1,213,727	1,213,727	964,931	964,931
Interest payable	579,886	579,886	824,086	824,086
Related parties	297,786	297,786	132,204	132,204
Accrued personnel costs	223,887	223,887	118,906	118,906
Retentions payable	32,577	32,577	75,985	75,985
Accrued utilities	26,366	26,366	19,585	19,585
Short-term debt	2,634,148	2,634,148	2,504,007	2,504,007
Current portion of long-term debt	9,512,760	9,512,760	9,359,594	9,359,594
Noncurrent Other Financial Liabilities				
Other noncurrent liabilities	6,817,643	6,823,734	6,141,065	5,744,879
Long-term debt	37,884,705	42,089,076	38,517,839	42,613,956
Cumulative redeemable preferred shares	–	–	2,500,000	2,790,743
Total other financial liabilities	₱79,071,741	₱83,282,203	₱77,318,524	₱81,309,198

The following methods and assumptions were used to estimate the fair value of each class of financial instrument for which it is practicable to estimate such value:

Cash and cash equivalents, short-term investments and current receivables - Carrying amounts approximate fair values due to the relative short-term maturities of these investments.

Financial assets at FVPL - These are investments in government securities and TRG fund (see Note 8). Fair value is based on quoted prices.

Noncurrent trade and nontrade receivables - The fair values are based on the discounted value of future cash flows using the applicable rates for similar types of instruments. The discount rates used ranged from 4.19% to 6.04% in 2007 and 5.0% to 6.7% in 2006.

AFS quoted equity shares - Fair values are based on quoted prices published in markets.



AFS unquoted shares - The fair value of unquoted shares are not reasonably determinable due to the unpredictable nature or future cash flows and the lack of suitable methods of arriving at a reliable fair value.

HTM investments - The fair value of bonds is based on quoted market prices.

Liabilities - The fair values of accounts payable and accrued expenses and short-term debt approximate the carrying amounts due to the short-term nature of these transactions.

The fair value of noncurrent other financial liabilities (fixed rate and variable rate loans repriced on a semi-annual/annual basis and deposits) are estimated using the discounted cash flow methodology using the current incremental borrowing rates for similar borrowings with maturities consistent with those remaining for the liability being valued. The discount rates used ranged from 4.19% to 6.04% in 2007 and 5.0% to 6.7% in 2006.

For variable rate loans that reprice every three months, the carrying value approximates the fair value because of recent and regular repricing based on current market rates.

The fair value of forward currency contracts is based on counterparty valuation except for forward transactions with a nonbank counterparty where valuation was calculated by reference to currency forward exchange rates for contracts with similar maturity profiles. The fair value of the outstanding structured currency option was derived from the mark-to-market valuations as provided by counterparty banks.

## **Risk Management and Financial Instruments**

### General

In line with the corporate governance infrastructure of the Company, the Company has adopted a group-wide enterprise risk management framework in 2002. An Enterprise Risk Management Policy was approved by the Audit Committee (the Committee) in 2003 and subsequently revised and approved on February 14, 2008. The policy was designed primarily to enhance the risk management process and institutionalize a focused and disciplined approach to managing the Company's business risks. By understanding and managing risks, the Company provides greater certainty and confidence to its shareholders, employees, customers and for the communities where the Company operates.

The risk management framework encompasses the following:

- identification and assessment of business risks;
- development of risk management strategies;
- assessment, design and implementation of risk management capabilities;
- monitoring and evaluating the effectiveness of risk mitigation strategies and management performance; and,
- identification of areas and opportunities for improvement in the risk management process.



A Chief Risk Officer is the ultimate champion of enterprise wide risk management and oversees the entire risk management function and is responsible for overall continuity. Beginning 2008, under its expanded charter, the Committee will provide a more focused oversight role over the risk management function. A quarterly report on the risk portfolio of the Group and the related risk mitigation efforts and initiatives are provided to the Committee. The Company's internal audit monitors the compliance with the Group's risk management policies in order to ensure that an effective control environment exists within the Group as a whole.

Financial Risk Management Objectives and Policies

The Group's principal financial instruments comprise of financial assets at FVPL, AFS financial assets, HTM investments, bank loans, corporate notes and bonds. The financial debt instruments were issued primarily to raise financing for the Group's operations. The Group has various financial assets such as cash and cash equivalents, accounts and notes receivables and accounts payable and accrued expenses which arise directly from its operations.

The main purpose of the Group's financial instruments is to fund its operational and capital expenditures. The main risks arising from the use of financial instruments are interest rate risk, foreign exchange risk, liquidity risk and credit risk. The Group also enters into derivative transactions, the purpose of which is to manage the currency and interest rate risk arising from its financial instruments.

The Group's risk management policies are summarized below:

*Interest Rate Risk*

The Group's exposure to market risk for changes in interest rates relates primarily to the Company's and its subsidiaries' long-term debt obligations. The Group's policy is to manage its interest cost using a mix of fixed and variable rate debt.

The following table demonstrates the sensitivity of the Group's profit before tax and equity to a reasonably possible change in interest rates on December 31, 2007, with all variables held constant.

	Change in basis points +100 basis points	
	<b>Effect on income before income tax</b>	<b>Effect on equity</b>
	(In Thousands)	
FVPL financial assets	(₱9,975)	(₱9,975)
Parent Company - floating rate borrowings	(57,817)	(37,581)
Subsidiaries - floating rate borrowings	(63,620)	(41,353)
	<b>(₱131,412)</b>	<b>(₱88,909)</b>



	Change in basis points -100 basis points	
	<b>Effect on income before income tax</b>	<b>Effect on equity</b>
	(In Thousands)	
FVPL financial assets	₱10,348	₱10,348
Parent Company - floating rate borrowings	57,817	37,581
Subsidiaries - floating rate borrowings	63,620	41,353
	<b>₱131,785</b>	<b>₱89,282</b>



The terms and maturity profile of the interest-bearing financial assets and liabilities, together with its corresponding nominal amounts and carrying values (in thousands), are shown in the following table:

2007

Group	Interest terms (p.a.)	Rate Fixing Period	Nominal Amount	< 1 year	1 to 5 years	> 5 years	Carrying Value
Cash and cash equivalents	Fixed at the date of investment	Various	₱36,835,549	₱36,835,549	₱–	₱–	₱36,835,549
Short-term investments	Fixed at the date of investment or revaluation cut-off	Balance date	3,687,606	3,687,606	–	–	3,687,606
FVPL financial assets	Fixed at the date of investment or revaluation cut-off	Balance date	622,097	622,097	–	–	622,097
Accounts and notes receivable	Fixed at the date of sale	Date of sale	13,656,785	10,181,479	3,475,306	–	13,656,785
HTM investments	Fixed at 16.50%	6 months	65,000	–	67,947	–	67,947
Company							
Long-term debt							
<i>Fixed</i>							
	Fixed at 6.70%	7 years	1,500,000	7,500	–	1,492,500	1,500,000
	Fixed at 6.73% to 10.00%	3 to 5 years	11,000,000	–	11,000,000	–	11,000,000
	Fixed at 10.38%	5 years	4,180,000	10,000	4,170,000	–	4,180,000
<i>Floating</i>							
	Variable at 0.50% to 1.50% over 91-day T-bills PDST-F (formerly Mart1)	3 months	7,129,091	665,606	973,485	5,490,000	7,129,091
Subsidiaries							
Short-term debt							
	Variable ranging from 3.10% to 6.40%	Monthly	390,248	390,248	–	–	390,248
	Variable ranging from 3.40% to 9.00%	Monthly	2,243,900	2,243,900	–	–	2,243,900
Long-term debt							
<i>Fixed</i>							
	Fixed at 8.125%	5 years	5,421,438	5,421,438	–	–	5,421,438
	Fixed at 5.0% to 14.88%	5, 7 and 10 years	6,246,759	1,167,460	3,899,624	1,175,295	6,242,379
<i>Floating</i>							
	Variable at 6.00% to 15.00%	3 months	9,639,933	331,943	9,307,990	–	9,639,933
	Variable at 1.00% to 1.50% over 91-day PDST-F or PDST-R1	3 months	2,288,840	1,209,140	879,412	196,072	2,284,624



2006

	Interest terms (p.a.)	Rate Fixing Period	Nominal Amount	< 1 year	1 to 5 years	> 5 years	Carrying Value
Group							
Cash and cash equivalents	Fixed at the date of investment	Various	₱20,391,301	₱20,391,301	₱-	₱-	₱20,391,301
Short-term investments	Fixed at the date of investment or revaluation cut-off	Balance date	2,927,928	2,927,928	-	-	2,927,928
FVPL financial assets	Fixed at the date of investment or revaluation cut-off	Balance date	2,302,694	2,302,694	-	-	2,302,694
Accounts and notes receivable	Fixed at the date of sale	Date of sale	12,711,196	10,644,524	2,126,672	-	12,771,196
HTM investments	Fixed at 16.50%	6 months	120,421	57,369	70,206	-	127,575
Company							
Long-term debt							
<i>Fixed</i>							
	Fixed at 10.00%	3 years	3,000,000	-	3,000,000	-	3,000,000
	Fixed at 10.375% to 10.60%	5 years	4,690,000	10,000	500,000	4,180,000	4,690,000
	Fixed at 10.60% to 12.00%	5 years	1,250,000	-	1,250,000	-	1,250,000
	Fixed at 11%	3 years	1,000,000	1,000,000	-	-	1,000,000
	Fixed at 12.68%	5 years	7,000,000	-	-	7,000,000	7,000,000
<i>Floating</i>							
	Variable ranging from 1.0% to 1.5% over 91-day PDST-F (formerly MART 1)	3 months	4,794,697	1,161,856	1,714,091	1,918,750	4,794,697
Subsidiaries							
Short-term debt							
	Variable ranging from 4.1% to 6.4%	Monthly	815,787	815,787	-	-	815,787
	Variable ranging from 6.1% to 7.8%	Monthly	1,688,220	1,688,220	-	-	1,688,220
Long-term debt							
<i>Fixed</i>							
	Fixed at 8.125%	5 years	6,706,393	-	6,706,393	-	6,706,393
	Fixed at 5.0% to 14.88%	3 to 10 years	5,942,568	175,100	4,010,846	1,750,000	5,935,946
<i>Floating</i>							
	Variable at 0.77% to 2.40% over 91-day PDST-F or PDST-R1	3 months	8,154,932	3,624,145	4,530,787	-	8,154,932
	Variable at 1.25% to 2.50% over 91-day PDST-F or PDST-R1	3 months	5,352,333	3,388,493	1,956,972	-	5,345,465



*Foreign Exchange Risk*

The Group's foreign exchange risk results primarily from movements of the Philippine Peso (PHP) against the United States Dollar (USD). The Company may enter into foreign currency forwards and foreign currency swap contracts in order to hedge its USD obligations.

The table below summarizes the Group's exposure to foreign exchange risk as of December 31, 2007 and 2006. Included in the table are the Group's assets and liabilities at carrying amounts, categorized by currency.

	2007		2006	
	USD	Php Equivalent	USD	Php Equivalent
	(In Thousands)			
<b>Assets</b>				
Cash and cash equivalents	\$347,032	₱14,332,164	\$148,272	₱7,276,454
Accounts and notes receivables	227,460	9,390,012	127,402	6,264,312
Other current assets	9,546	394,072	16,447	810,372
Investment in bonds and other securities	91,135	3,899,746	21,785	1,068,397
Other noncurrent assets	23,541	990,947	72,868	3,558,460
<b>Total assets</b>	<b>698,714</b>	<b>29,006,941</b>	<b>386,774</b>	<b>18,977,995</b>
<b>Liabilities</b>				
Accounts payable and accrued expenses	87,947	3,631,016	54,521	2,686,122
Other current liabilities	5,887	243,024	80,842	3,966,758
Short-term debt	9,454	390,248	10,016	493,571
Long-term debt	233,526	9,639,934	236,227	11,602,661
Other noncurrent liabilities	159	6,599	1,696	83,212
<b>Total liabilities</b>	<b>336,973</b>	<b>13,910,821</b>	<b>383,302</b>	<b>18,832,324</b>
<b>Net foreign currency denominated assets</b>	<b>\$361,741</b>	<b>₱15,096,120</b>	<b>\$3,472</b>	<b>₱145,671</b>

The following table demonstrates the sensitivity to a reasonably possible change in the US dollar rate, with all variables held constant, of the Group's profit before tax (due to changes in the fair value of monetary assets and liabilities) and the Group's equity.

	US\$ depreciates (appreciates)	Effect on profit before tax	Effect on equity
2007	₱1.00 (₱1.00)	(361,741) 361,741	(235,132) 235,132

*Liquidity Risk*

The Group seeks to manage its liquidity profile to be able to service its maturing debts and to finance capital requirements. The Group maintains a level of cash and cash equivalents deemed sufficient to finance operations. As part of its liquidity risk management, the Company regularly evaluates its projected and actual cash flows. It also continuously assesses conditions in the financial markets for opportunities to pursue fund-raising activities. Fund-raising activities may include bank loans and capital market issues both on-shore and off-shore.



The table summarizes the maturity profile of the Group's financial liabilities as of December 31, 2007 and 2006 based on contractual undiscounted payments.

	<b>2007</b>				<b>Total</b>
	<b>&lt; 1 year</b>	<b>1 to &lt; 2 years</b>	<b>2 to &lt; 3 years</b>	<b>&gt; 3 years</b>	
	(In Thousands)				
Accounts payable and accrued expenses					
Accounts payable	₱13,289,481	₱-	₱-	₱-	₱13,289,481
Accrued expenses	6,558,775	-	-	-	6,558,775
Dividends payable	1,213,727	-	-	-	1,213,727
Interest payable	579,886	-	-	-	579,886
Related parties	297,786	-	-	-	297,786
Accrued personnel costs	223,887	-	-	-	223,887
Retentions payable	32,577	-	-	-	32,577
Accrued utilities	26,366	-	-	-	26,366
Short-term debt	2,634,148	-	-	-	2,634,148
Long-term debt	9,512,760	2,286,464	4,600,754	30,997,487	47,397,465
Other noncurrent liabilities	-	5,473,515	1,214,742	129,386	6,817,643
	<b>₱34,369,393</b>	<b>₱7,759,979</b>	<b>₱5,815,496</b>	<b>₱31,126,873</b>	<b>₱79,071,741</b>

	<b>&lt; 1 year</b>	<b>1 to &lt; 2 years</b>	<b>2 to &lt; 3 years</b>	<b>&gt; 3 years</b>	<b>Total</b>
Interest payable	₱1,856,769	₱1,646,875	₱1,518,916	₱ 2,894,524	₱7,917,084

	<b>2006</b>				<b>Total</b>
	<b>&lt; 1 year</b>	<b>1 to &lt; 2 years</b>	<b>2 to &lt; 3 years</b>	<b>&gt; 3 years</b>	
	(In Thousands)				
Accounts payable and accrued expenses					
Accounts payable	₱11,505,755	₱-	₱-	₱-	₱11,505,755
Accrued expenses	4,654,567	-	-	-	4,654,567
Dividends payable	964,931	-	-	-	964,931
Interest payable	824,086	-	-	-	824,086
Related parties	132,204	-	-	-	132,204
Accrued personnel costs	118,906	-	-	-	118,906
Retentions payable	75,985	-	-	-	75,985
Accrued utilities	19,585	-	-	-	19,585
Short-term debt	2,504,007	-	-	-	2,504,007
Long-term debt	9,359,594	11,988,994	10,340,704	16,188,141	47,877,433
Cumulative redeemable preferred shares	2,500,000	-	-	-	2,500,000
Other noncurrent liabilities	-	4,796,938	1,214,741	129,386	6,141,065
	<b>₱32,659,620</b>	<b>₱16,785,932</b>	<b>₱11,555,445</b>	<b>₱16,317,527</b>	<b>₱77,318,524</b>

### *Credit Risk*

The Group's holding of cash and short-term investments exposes the Group to credit risk of the counterparty. Credit risk management involves dealing only with institutions for which credit limits have been established. The treasury policy sets credit limits for each counterparty. Given the Group's diverse base of counterparties, it is not exposed to large contractions of credit risk.



The table below shows the maximum exposure to credit risk for the components of the consolidated balance sheet. The maximum exposure is shown at gross, before the effect of mitigation through the use of master netting arrangements or collateral agreements.

	2007	2006
	(In Thousands)	
Cash and cash equivalents	<b>₱36,835,549</b>	₱20,391,301
Short-term investments	<b>3,687,606</b>	2,927,928
FVPL financial assets		
Financial assets at FVPL	<b>622,097</b>	2,302,694
Derivative assets	<b>143,322</b>	-
Accounts and notes receivables		
Trade		
Real estate	<b>9,293,014</b>	7,710,190
Electronics manufacturing	<b>2,941,419</b>	3,213,056
Information technology and business process outsourcing	<b>343,977</b>	239,018
Automotive	<b>753,661</b>	493,287
International and others	<b>5,783</b>	3,010
Advances	<b>2,231,057</b>	2,280,965
Related parties	<b>2,395,624</b>	1,935,112
Dividends	-	1,262,538
Others	<b>1,947,658</b>	2,176,696
AFS investments		
Quoted shares of stocks	<b>2,166,168</b>	2,373,486
Unquoted shares of stocks	<b>258,798</b>	961,374
Held-to-maturity investments		
Bonds	<b>67,947</b>	127,575
<b>Total credit risk exposure</b>	<b>₱63,693,680</b>	<b>₱48,398,230</b>



The analysis of accounts and notes receivables that were past due but not impaired follows:

December 31, 2007

	Neither Past Due nor Impaired	Past Due but not Impaired					Total	Impaired	Total
		<30 days	30-60 days	60-90 days	90-120 days	>120 days			
(In Thousands)									
Trade:									
Real estate	₱7,770,857	₱862,024	₱240,163	₱119,959	₱225,138	₱162,262	₱1,609,546	₱32,119	₱9,412,522
Electronics manufacturing	2,808,752	112,452	6,636	3,590	8,999	990	132,667	31,180	2,972,599
Automotive	529,296	112,582	75,724	34,662	14,975	12,529	250,472	–	779,768
Information technology and business process outsourcing	275,986	15,379	23,194	2,901	7,732	18,785	67,991	18,261	362,238
International and others	–	3,465	2,019	–	415	910	6,809	60,134	66,943
Advances	1,823,158	58,432	96,265	92,315	83,532	77,355	407,899	–	2,231,057
Related parties	2,060,190	49,694	36,372	36,217	35,691	177,460	335,434	–	2,395,624
Others	1,596,634	37,824	36,835	38,085	48,433	143,779	304,956	232,256	2,133,846
<b>Total</b>	<b>₱16,864,873</b>	<b>₱1,251,852</b>	<b>₱517,208</b>	<b>₱327,729</b>	<b>₱424,915</b>	<b>₱594,070</b>	<b>₱3,115,774</b>	<b>₱373,950</b>	<b>₱20,354,597</b>



The table below shows the credit quality of the Group's financial assets as of December 31, 2007 (in thousands):

	Neither past due nor impaired			Total	Past due but	Impaired	Total
	High Grade	Medium Grade	Low Grade		not impaired		
Cash and cash equivalents	₱36,835,549	₱—	₱—	₱36,835,549	₱—	₱—	₱36,835,549
Short-term investments	3,687,606	—	—	3,687,606	—	—	3,687,606
FVPL financial assets					—	—	
Financial assets at FVPL	622,097	—	—	622,097	—	—	622,097
Derivative assets	143,322	—	—	143,322	—	—	143,322
Accounts and notes receivables							
Trade							
Real estate	5,294,456	1,748,757	727,644	7,770,857	1,609,546	32,119	9,412,522
Electronics manufacturing	1,307,280	1,025,486	475,986	2,808,752	132,667	31,180	2,972,599
Information technology and business process outsourcing	—	275,986	—	275,986	67,991	18,261	362,238
Automotive	329,296	200,000	—	529,296	250,472	—	779,768
International and others	—	—	—	—	6,809	60,134	66,943
Advances	1,743,470	79,688	—	1,823,158	407,899	—	2,231,057
Related parties	2,056,364	3,826	—	2,060,190	335,434	—	2,395,624
Others	1,106,199	241,517	248,918	1,596,634	304,956	232,256	2,133,846
AFS Investments							
Quoted shares of stocks	2,033,594	132,574	—	2,166,168	—	—	2,166,168
Unquoted shares of stocks	—	258,798	—	258,798	—	—	258,798
HTM Investments							
Quoted debt investments	67,947	—	—	67,947	—	—	67,947
	₱55,227,180	₱3,966,632	₱1,452,548	₱60,646,360	₱3,115,774	₱373,950	₱64,136,084



The credit quality of the financial assets was determined as follows:

Cash and cash equivalents, short-term investments, FVPL financial assets, quoted AFS investments and HTM investments - based on the nature of the counterparty and the Group's internal rating system.

Receivables:

Real estate - high grade pertains to receivables with no default in payment; medium grade pertains to receivables with up to 3 defaults in payment; and low grade pertains to receivables with more than 3 defaults in payment.

Electronics manufacturing - high grade pertains to receivable with favorable credit terms and can be offered with a credit term of 15 to 45 days; medium grade pertains to receivable with normal credit terms and can be offered with a credit term of 15 to 30 days; and low grade pertains to receivables under advance payment or confirmed irrevocable Stand-by Letter of Credit and subjected to semi-annual or quarterly review for possible upgrade.

Automotive - high grade pertains to receivables from corporate accounts and medium grade for receivables from noncorporate accounts.

Available-for-sale investments - the unquoted investments are unrated.

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### 30. Registration with the Philippine Export Zone Authority (PEZA)

Some activities of certain subsidiaries are registered with the PEZA. Under the registration, these subsidiaries are entitled to certain tax and nontax incentives, which include, but are not limited to, income tax holiday (ITH) and duty-free importation of inventories and capital equipment. Upon the expiration of the ITH, the subsidiaries will be liable for payment of a five percent (5%) tax on gross income earned from sources within the PEZA economic zone in lieu of payment of national and local taxes.

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### 31. Note to Consolidated Statements of Cash Flows

Noncash investing activities are as follows:

	2007	2006	2005
		(In Thousands)	
Property/liquidating dividend	₱—	₱16,573	₱—
Acquisitions through issuance of shares of stock of a subsidiary	—	—	776,985



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## 32. Commitments and Contingencies

### Commitments

ALI has an existing contract with the Bases Conversion Development Authority (BCDA) to develop, under a lease agreement, a mall with an estimated gross leasable area of 152,000 square meters on a 9.8-hectare lot inside Fort Bonifacio. The lease agreement covers 25 years, renewable for another 25 years subject to reappraisal of the lot at market value. The annual fixed lease rental amounts to ₱106.5 million while the variable rent ranges from 5% to 20% of gross revenue. Subsequently, ALI transferred its rights and obligations granted to or imposed under the lease agreement to SSECC, its subsidiary, in exchange for equity.

As part of the bid requirement, ALI procured a performance bond in 2003 from the Government Service Insurance System in favor of BCDA amounting to ₱3.9 billion to guarantee the committed capital to BCDA. Moreover, ALI obtained surety bonds to guarantee the payment of the fixed and variable rent as prescribed in the lease agreement. The surety bonds are secured by a mortgage on a property of a certain subsidiary with a carrying value of ₱48.6 million in 2004.

On April 15, 2003, ALI entered into a Joint Development Agreement (JDA) with BCDA for development of another lot inside Fort Bonifacio with a gross area of 11.6 hectares for residential purposes. Pursuant to the agreement, BCDA shall contribute its title and interest to the lot and ALI in turn shall provide the necessary cash and expertise to undertake and complete the implementation of the residential development. ALI commits to invest sufficient capital to complete the residential development.

ALI procured a surety bond with a face value of ₱122.9 million issued by an insurance company in favor and for the benefit of BCDA as beneficiary. The surety bond shall be continuing in nature and shall secure the obligation of ALI to pay BCDA annual minimum revenue share for each of the first 8 selling periods of the residential project.

In 2002, ALI agreed to underwrite the subscription to NTDCC additional shares amounting to ₱1.4 billion over a 4-year equity schedule up to 2007 in exchange for a 5% underwriting fee (net of a 1.5% rebate to existing shareholders who subscribed).

### Contingencies

The Group has various contingent liabilities arising in the ordinary conduct of business which are either pending decision by the courts or being contested, the outcome of which are not presently determinable.

Avida Land Corp. (Avida), a wholly owned subsidiary of ALI, is involved in a patent infringement suit brought by plaintiffs Edgardo Vasquez and Vasquez Building Systems Corporation against Avida. The Plaintiff alleged that Avida infringed on Vasquez's modular housing unit patent. Avida had raised a number of defenses, including (a) it makes use of patented technology licensed from UK and French Companies, and not Vasquez's modular housing unit patent; (b) the Vasquez patent claim is overboard, since the patent does not protect the H-shaped column and the wall panel installation system; and (c) the H-shaped column and the wall panel installation system cannot be covered by the Vasquez patent, because these are not patentable as they do not qualify on "novelty."



In a decision dated December 18, 2007, the Regional Trial Court of Quezon City found in favor of the plaintiffs and rendered the following awards against Avida: (a) ₱90.0 million as temperate damages or reasonable royalty with interest at the rate of six percent (6%) per annum reckoned from the date of filing of the verified Complaint, December 19, 1999, until the same is fully paid; (b) ₱5.0 million as moral damages; (c) ₱1.0 million as exemplary damages; (d) ₱0.5 million as reasonable attorney's fees and expenses of litigation; and (e) costs of suit.

Although the decision was against Avida, the overwhelming strength of Avida's defenses which were arbitrarily disregarded by the Trial Court has prompted Avida's management to seek relief from a higher court. Hence, on January 4, 2008, Avida filed an appeal to contest this decision, intending to elevate this case to the Court of Appeals.

In the opinion of management and its legal counsel, the eventual liability under these lawsuits or claims, if any, will not have a material or adverse effect on the Group's financial position and results of operations. No provisions were made during the year. The information usually required by PAS 37/IAS 37, *Provisions, Contingent Liabilities and Contingent Assets*, is not disclosed on the grounds that it can be expected to prejudice the outcome of these lawsuits, claims and assessments.

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### 33. Subsequent Event

As a result of the explosion which occurred on October 19, 2007 at the basement of the Makati Supermarket Building, the Philippine National Police (PNP) has recommended to the Department of Justice (DOJ), in its report dated January 11, 2008, the prosecution of certain officers/employees of Makati Supermarket Corporation, the owner of the building, as well as some officers/employees of ALI's subsidiary, Ayala Property Management Corp. (APMC), among other individuals, for criminal negligence. No criminal case has been filed by the DOJ at this time. No civil case has likewise been filed by any of the victims. In the event that the DOJ decides to file a criminal case against certain officers/employees of APMC as recommended by the PNP, the accused, if convicted after final judgment, can be held not only criminally but also civilly liable. In the event the accused will not be able to pay for the civil award, APMC will be held subsidiarily liable for such sums (the amount of which cannot be estimated). ALI and APMC believe, however, that the facts surrounding the incident do not show any negligence.

